New England Journal of Entrepreneurship

Volume 9 | Number 1 Article 1

2006

# New England Journal of Entrepreneurship, Spring 2006

# New England Journal of Entrepreneurship

Spring 2006 Volume 9 Number 1



NEJE

John F. Welch College of Business SACRED HEART UNIVERSITY

New England Journal of Entrepreneurship



*New England Journal of Entrepreneurship* is a semi-annual publication (Fall and Spring) of the John F. Welch College of Business, Sacred Heart University, 5151 Park Avenue, Fairfield, CT 06825-1000.

Annual subscription rate for two issues is $12.00 for individuals and $50.00 for institutions. Copies are mailed via second-class postage.  Library of Congress ISSN 1550-333X.
For subscriptions or reprints of articles, call (203) 371-7854 or email: shuartj@sacredheart.edu.

**Editorial Consultant: Miccinello Associates, Branford, CT.**

# New England Journal of Entrepreneurship

Spring 2006 Volume 9 Number 1

# New England Journal of Entrepreneurship

## Call for Articles

*New England Journal of Entrepreneurship (NEJE)*, published twice a year by Sacred Heart University's John F. Welch College of Business, is an invaluable forum for exchange of scholarly ideas, practices, pedagogy, and policies in the field of entrepreneurship and small business management.

The *Journal* is currently seeking original contributions that have not been published or are under consideration elsewhere. The scope of the articles published in *NEJE* range from theoretical/conceptual to empirical research, with maximum relevance to practicing entrepreneurs. The *Journal* will consider practitioner interviews, book reviews, experiential exercises, cases, and articles dealing with entrepreneurial education. The *Journal* appeals to a broad audience, so articles submitted should be written in such a manner that those outside of academics would be able to comprehend and appreciate the content of the material.

## Format

Manuscripts submitted to NEJE should be written in Microsoft Word or saved in RTF (rich text format). All papers should be submitted electronically, via e-mail attachment, to hsherman@southampton.liu.edu.

Accompanying each manuscript, as a separate file, should be (a) an abstract of the article (100 words maximum), (b) a biographical sketch of the author(s), and (c) a page with manuscript title and the order of authors as well as the primary author's name, mailing address, preferred e-mail, phone and fax numbers.

Authors' names should not appear anywhere in the manuscript including Word document properties.

Papers are to be double-spaced with one-inch margins. References should be included on separate pages at the end of the paper. Manuscripts should he no longer than 20 pages of text and 25 pages total, including abstract, text, tables or illustrations, notes, and works cited. Please consult APA style guidelines for all formatting details.

## Copyright

The copyright of published articles will belong to the publishers of *NEJE.* Authors will be granted permission to reprint or otherwise use portions of their articles published in the *Journal* upon written request.

## Review Process

All articles will be double-blind refereed. Authors will normally receive reviewers' comments and the editors' publishing decision in approximately 90 days of submission.

## Submission

All snail-mail correspondence should be addressed to:

Herbert Sherman, Ph.D.
Editor, New England Journal of Entrepreneurship
Southampton College—Long Island University
239 Montauk Highway
Southampton, NY 11968
Phone: (631) 287-8285
Fax: (631) 287-8441
e-mail: hsherman@southampton.liu.edu

Visit our web page at http://business.sacredheart.edu/neje.html

## Sample Copies

Sample copies of previous issues are available from Joshua Shuart, Associate Editor, on a first-come, first-served basis.
Please contact him via e-mail at shuartj@sacredheart.edu.

# New England Journal of Entrepreneurship

## From the Editors:

In the Spring 2005 issue we announced that Dr. Lorry Weinstein, co-founder and editor of the *Journal*, was retiring as editor and that an interim editor would shortly be named. We would like to thank Dr. Weinstein for his arduous and ardent efforts on behalf of the *Journal* and note that he will continue to remain on the editorial board. We would also like to thank Dr. Herbert Sherman of Southampton College, Long Island University, for taking on the onerous task of interim editor. Dr. Sherman has served as the editor of the *Journal of Behavioral and Applied Management* and has just retired as the founding editor of the *CASE Journal.* Both are online journals and he looks forward to working on a hardcopy one.

You may have noticed when you perused the front and inside cover of this issue that we have instituted some new and, we hope, creative and stimulating changes. It is our intention and fervent wish to position the journal as a bridge between academics and practitioners and, within the academic community, a bridge between researchers and instructors. To carry out this mission, we have segmented the journal into several topical areas including book reviews, minority and women entrepreneurs, entrepreneurial education, practitioner's corner, practitioner's interviews, and international entrepreneurship and appointed an associate editor in charge of each area. We hope to have at least one manuscript published in each area per issue, therein creating a balanced arrangement.

The associate editors have been charged with the task of soliciting manuscripts for their area and managing the review process. The editor will forward manuscripts received through the normal solicitation process to them as per their subject area. Manuscripts that fall outside of their jurisdiction will be processed, as before, by the editor. Manuscripts that are accepted by the associate editors will be featured in their own section of the *Journal,* with an accompanying note from the associate editor.

This issue features five articles and one case. The first article written by Rolland LeBrasseur, Huguette Blanco, and John Dodge of Laurentian University, entitled "Growth Intentions of Owner-Managers of Young Microfirms," is an empirical piece, which examines the intended growth of young microfirms and postulated that these firms could be categorized as either Lifestylers, Entrepreneurs, Managers, or Movers. Their research indicated that this typology was accurate and furthermore that government and nonprofit agencies supporting business growth should take these characteristics into account when providing assistance.

Maria Minniti of Babson College also examined government support for entrepreneurial activities in the second article, entitled "A Cross-Country Assessment of Government Intervention and Entrepreneurial Activity." This empirical study, employing original data from a representative sample of 10,000 individuals and from more than 300 semi-open interviews in 10 countries, provides some suggestive evidence that government intervention aimed at enhancing the underlying environment of entrepreneurial decisions may be more effective than intervention designed to provide safety nets.

We go from macro empirical research to a micro two-part field-based disguise case when Herbert Sherman, Southampton College–Long Island University, and Daniel J. Rowley, University of Northern Colorado, present a rather intriguing real-life situation: What do you do if you run a family firm, hired your only progeny to run the business, and then had that offspring quit a few days later? There are some challenging twists and turns in this case as Part B provides the reader with additional information that turns the case (and the situation) on its head!

The next two articles—"Capital Accessibility, Gender and Ethnicity: The Case of Minority Women-Owned Firms" by Leyland M. Lucas, Morgan State University and "The Embedded Entrepreneur: Recognizing the Strength of Ethnic Social Ties" by Ed Chung and Kim Whalen, Elizabethtown College—deal with gender and ethnicity issues and are described by our associate editor, Miles K. Davis. Last, but never least, Joseph E. Levangie has again graced us with another practitioner article as he has teamed up with Deaver Brown of *Simply Magazine* to tell us all about sales through the imagery of the purchase order in the article entitled "The Often-Neglected Term in the Entrepreneurial Equation—the Purchase Order." Joe has also provided us some chance pearls of wisdom in the introduction to the article.

We look forward to hearing from you, our readership, concerning these changes and would appreciate your feedback and suggestions.

Herbert Sherman
Editor

Joshua Shuart
Associate Editor and Web Master

Lorry Weinstein
Editor Emeritus

New England Journal of Entrepreneurship

## From the Associate Editors:

### Joseph E. Levangie—The Practitioner's Corner

The Practitioner's Corner has been edited for the last two years by Joseph E. Levangie who has nearly three decades of entrepreneurial experience. Joe has been involved in more than five dozen start-ups, has helped raise over $600 million for these emerging ventures, including a dozen public capital raise-ups. He has observed the "good, the bad and the ugly" of entrepreneurship. He has personally contributed six articles to *NEJE*.

The Practitioner's Corner encompasses subject areas that reflect the actual touch and feel of the entrepreneurial experience. Candidate manuscripts should address a practical concern for the entrepreneur or those interested in real-world aspects of the venturing challenge, including functional concerns (finance, sales, planning, outsourcing, etc.); psychological issues (motivational factors, risk assessment, decision making, etc.); and insights into a changing entrepreneurial environment (new laws and regulations, the rise of China, etc.). Manuscripts should be 12–30 pages in length, include citations for references to quotes and factual data and be written in a style appealing to the practicing entrepreneur or followers of the genre.

In this issue, I collaborated with a long-time colleague, Deaver Brown, to address how businesses should "make sales happen" in our article entitled "The Often-Neglected Term in the Entrepreneurial Equation—the Purchase Order." I warn you that Brown's elitist education (Choate, Harvard College, Harvard Business School) should not be interpreted as a lack of "street smarts"; Brown's more entrepreneurially friendly credentials include winning Golden Gloves boxing medals and selling Fuller Brush products door-to-door! To ascertain how the entrepreneur can wrest an order from a prospective customer, read on!

### Miles K. Davis—Minority and Women Entrepreneurs

As a new associate editor at *NEJE,* I would like to briefly introduce myself. I am an associate professor of management at Shenandoah University and the director of the Institute for Entrepreneurship. In my academic and professional life, I strive to bridge the gap that sometimes exists between theory and practice. The articles in this section are examples of the kind of scholarship that does just that.

While it is assumed that minority women-owned business are undercapitalized as a result of bias and discriminatory practices in capital markets, Leyland M. Lucas of Morgan State University in the article entitled "Capital Accessibility, Gender and Ethnicity: The Case of Minority Women-Owned Firms" makes a compelling argument that in practice the issues are much more complex. He argues that while discrimination may exist, most financing institutions are behaving as they should and the lack of capital access is more explained by inexperience, information inaccessibility, and liabilities of newness and size. Whether you agree or disagree with the hypotheses offered by Dr. Lucas, this article will certainly add to the debate regarding financing of minority women-owned businesses.

Ed Chung and Kim Whalen of Elizabethtown College in their article, "The Embedded Entrepreneur: Recognizing the Strength of Ethnic Social Ties," premised on the idea that social networks represent an important, but often overlooked, unit of analysis in management and entrepreneurship studies. The concept of embeddedness, emphasizing the significance of social relationships, is of particular relevance as more and more frequently minorities and immigrants engage in small business ownership. This article borrows from the ethnicity and social network traditions, and offers that an analysis of the ethnic homogeneity of an entrepreneur's strong and weak social ties would be fruitful in gauging entrepreneurial success.

I hope if you have a thought-provoking, challenging issue regarding women and minority entrepreneurs, you will submit your scholarly work to *NEJE*. If you wish to contact me directly regarding whether an article is suitable, I can most easily be reached by email at mdavi3@su.edu and every once in awhile I am actually in my office (540) 545-7314.

## Barry R. Armandi—Book Reviews

Welcome to the book reviews section of the *NEJE*. Our purpose in this section is to present reviews of not only current books in the field, but also other materials such as case books, simulations, and exercises. We would also encourage reviews of classic books and materials.

Two problems, however, have been identified to get the book reviews section off the proverbial ground. First, we need reviewers. Reviewing is not the laborious process many of us have felt in the past. We have created guidelines not only to aid in reviewing, but also to standardize our reviews. The guidelines are posted on our website for easy downloading. If you wish to review, please send an email to the address at the bottom of this introduction.

The second problem is coverage of the field. We would like you to recommend works that should be reviewed. We have a number in the pipeline already, and if there is duplication, we'll let you know. Likewise, if there are some older "classic" materials you use or wish to see reviewed, then again please contact us. Once you make a recommendation, hopefully you will want to do the review.

I look forward to hearing from you (armandi@attglobal.net or armandib@oldwestbury.edu).

## Pamela Hopkins—Entrepreneurial Education

Are you interested in finding new ways to make learning environments exciting yet still challenging and stimulating to the students and to you? Would you like to discuss new techniques with your colleagues? Would it be exciting to hear about students' experiences in these dynamic classrooms from the students themselves? Or what about sharing entrepreneurial education experiences using online instruction?

As associate editor of entrepreneurship education, my goal is to report these learning techniques and experiences so that we all may grow as teachers. I see this as a forum whereby we are discussing cutting-edge entrepreneurship education—maybe it is an idea, an application, an experiment, or a critique.

Entrepreneurs tell us many times that their successful ventures came about after a failure. I believe it is the same with entrepreneurial professors, who are always venturing to try new teaching methods and techniques. So, even if you think your attempt was unsuccessful, I think it is worthy to read about why. Maybe a tweak here and there through our discussion or even a change of venue can bring about success.

I am Pamela J. Hopkins and have been a professor for the past 26 years, currently teaching management at Southern Connecticut State University. As the associate editor of entrepreneurship education, I invite you to join me in creating a forum whereby we can share and discuss classroom experiences. With the acceleration of technology combined with diverse ways of student learning, a variety of exciting venues exist for us to explore.

This is a call for papers that explore creative and innovative approaches to entrepreneurial education. This is a call to all those teachers who are experimenting with accomplishing learning outcomes. If you enjoy this education experiment, please take the time to write up your experience so we can share and learn.

## Daniel J. Rowley—Practitioner Interviews

Daniel J. Rowley is a professor of management and chair of the Management Department at the Monfort College of Business at the University of Northern Colorado. He is the lead author of four scholarly books on strategic planning in colleges and universities; a workbook in the same series; a book on academic supervision; and a forthcoming textbook on business strategic management with Dr. Sherman. He is the author of articles and presentations on these subjects nationally and internationally. He has served as editor and as associate editor of the *Journal of Behavioral and Applied Management,* and has published book reviews and article reviews in several different journals. He received his B.A. from the University of Colorado at Boulder in 1969; his MPA from the University of Denver in 1978; and his Ph.D. from the University of Colorado at Boulder in 1987.

Practitioner interviews need to be objective and less personal in approach. Accolades for experience, position, and power should be placed either in the introduction or in the final biographical piece. They should not be placed within the body of the discussion. The interview must focus on what the entrepreneur has deduced about entrepreneurialism and how he or she has used it specifically in his or her career. To me, being able to show how entrepreneurialism has been a significant player is of extreme interest to the readers of an academic journal. See prior issues and our website for examples.

## Gerry W. Scheffelmaier—International Entrepreneurship

Gerry W. Scheffelmaier is an assistant professor of entrepreneurship with a Ph.D. in business information systems from Utah State University, an M.Ed. in business and marketing and a B.S. in accounting from Central Washington University. His interests include buyer behavior and e-commerce. Dr. Scheffelmaier has employed the "Baseball Model" to describe a business start-up or failing e-commerce businesses. In the model, each base on the baseball diamond is occupied by one of three components necessary to establish, create, and implement a successful e-commerce business.

*NEJE* is quite interested in receiving any articles that deal with international entrepreneurship—that is, any article dealing with U.S. entrepreneurs working outside of the states as well as any articles pertaining to non-U.S. entrepreneurial ventures. Both conceptual and empirical articles are encouraged as well as international case studies.

# Growth Intentions of Owner-Managers of Young Microfirms

Rolland LeBrasseur
Huguette Blanco
John Dodge

*A survey of young microfirms was conducted to investigate their growth intentions. The findings confirm the distinct profiles of four types of firms categorized on the basis of current and future employment: Lifestyler, Entrepreneur, Manager, and Mover. They differ in terms of the owner's perceptions of the desirability and practicality of growing their firm, and with respect to the moderating variables of industry affiliation, business location, and investment level. Research issues and service implications for business support agencies are identified.*

Over the past few years, private and public resources have been expended to help entrepreneurs move from the idea stage to the start-up stage and survive their initial years of operation. In contrast, research and practices to help young firms in the initial growth stage has lagged (Chaganti et al. 2002; White 2002). Given the current state of knowledge, a descriptive study of initial growth would be a positive contribution to our understanding of the issues.

The purpose of the study is to identify the characteristics of young firms that are likely to experience growth. The study is guided by a typology of young firms that differentiates them on the basis of current and future levels of employment. Growth intentions are investigated using the Shapero-Krueger Model (Krueger et al. 2000) that focuses on the perceptions of the businessowners in terms of the desirability and practicality of growing their young enterprises, and the impact of moderating variables. The end result is a profile of four types of young firms and a discussion of service implications for the small business support agencies.

## Diversity within the Small Business Sector

In Canada, as well as in other industrialized countries, small businesses have replaced large firms as the motor of economic development, hence the interest in improving the survival rate of business start-ups (OECD 2000; Industry Canada 1996). By their very nature, small businesses are well suited to meeting the challenges of a changing economy because they can sustain an innovative and entrepreneurial spirit while remaining agile and adaptive to change (Industry Canada 2002).

Based on surveys executed by Statistics Canada, Industry Canada (2003) reported that microenterprises (0–4 employees) accounted for 19 percent of all businesses. Microenterprises are distributed broadly across both the goods-producing and service-producing sectors of the economy, but are predominant in construction, retail trade, business services, and consumer services.

The number of self-employed persons has grown substantially in the 1980s and 1990s (Industry Canada 2003, Table 10; Stanworth and Stanworth 1995). Of the self-employed people in Canada, 34 percent made use of paid help as either employees or contract staff. This statistic suggests that some of these one-person enterprises are evolving into employee-based enterprises. Self-employed persons are not likely to become paid employees of another firm (Dennis and Solomon 2001), as they have chosen this vocation. However, they are not a homogeneous group, and are driven by motives such as autonomy and independence, creativity, and security and stability (Feldman and Bolino 2000).

Working with small firms with fewer than 500 employees, Rutherford, McMullen, and Oswald (2001) have confirmed that discriminators based on the characteristics of the entrepreneur and of the firm (i.e., firm age) can be used to identify two groups of small businesses. They suggested additional investigation to identify subgroups of small firms. This suggestion, derived from their study of established firms, may be pertinent to the young and developing firms, which may form a distinct group with its own subgroups (e.g., small v. micro, industry). The academic literature typically explains the behavior of the young firms in terms of stage of development [see Ardichvili et al. (1998) for a review of a variety of models]. In contrast, Chrisman et al. (1998) presented a model for new firms anchored in the strategic literature. Chrisman's model is appealing because it covers both internal and external factors that may influence the competitive success of the young enterprise. Also, Chrisman et al. define "new" as less than 10 years in operation, arguing that there are unique circumstances in the first decade of a firm's existence (e.g., establishing core competencies). The cut-off of the first decade is validated by the survival statistics noted in the Industry Canada study (2003), which showed that it takes about 10 years for the microfirms to improve their survival rate to the survival rate of larger firms with 5 to 99 employees. The Industry Canada study also showed that microfirms have a relatively low survival rate in their first year of operations, thus justifying the focus of this study to microfirms 2 to 10 years old.

## Growth of Small Businesses

Growth in a firm may be defined alternatively as the rate of increase in sales volume or the rate of increase in the number of employees experienced by the firm. Both measures of growth are considered important, but the addition of employees, especially the initial employees, may be a greater challenge for the young firm. Since small businesses are usually defined in term of employment (see discussion above), growth in this article refers to increasing the employment level of the firm.

The attention of interested observers, such as lending institutions and economic development agencies, has recently been captured by hypergrowth and the "gazelle" (Birch et al. 1999; Rumball 2001). In a recent study of the Canadian economy, Halabisky, Dreessen, and Parsley (2004) confirmed that the "gazelles" are the star contributors to employment growth. However, the authors also stressed that the Canadian economy has reaped substantial benefits from small businesses that experience strong, but not hyper, growth. It can be argued that pacing the growth of the young firm may be a wise decision for owners who need more time to assess the growth opportunities and build the business to exploit these opportunities. However, economic developers view the young firm that limits itself to a one-person operation as a poor investment target. Morrison, Breen, and Ali (2003) argued that, because of limited supply, public resources should be directed to young firms that are likely to create employment. How can we best identify which young microfirms are likely to create employment?

The diverse approaches to explaining firm growth recognize the interdependence of the businessowner and the enterprise created. Cope and Watts (2000, p. 108) argued "that there exists a complex, interactive and mutual relationship between the individual and the organization, where entrepreneurs actively share their learning with their business, both shaping its growth and direction and passively adapting to the changing demands of the enterprise." It follows that in order to study growth of the small firm, personal, business, and industry variables must be addressed simultaneously.

## Growth Intentions in Small Business Start-ups

Researchers generally agree that growth in the firm is deliberate, and depends on the owner's mindset composed of his or her business vision, personal motivations, attitudes, and perceptions. The mind becomes focused through entrepreneurial intentions that guide the owner's decisions and actions. Bird (1988, 1992) described this concept as a cognitive tension between the business vision and current conditions. She proposed that the owner's intentions could be a key determinant of organizational success and growth.

Wiklund et al. (1997) concluded that growth intentions were moderately strong predictors of goal-directed behavior (Doll and Ajzen 1992; Kim and Hunter 1993). Kim and Hunter (1993) and Armitage and Conner (2001) have demonstrated through meta-analysis that intentions can successfully predict a wide variety of individual behaviors. With respect to firm performance, Orser et al. (1998) found a significant relationship between the owner's growth willingness (an indication of intention) and actual firm growth over a four-year period. Other researchers have confirmed that growth intentions prove to be better predictors of actual business growth for a distant horizon than for growth in the immediate future (Autio et al. 1997; Krueger et al. 2000; Reitan 1996).

Two similar but competing cognitive theories of intentions are present in the literature. First to appear was the cognitive theory of planned behavior (Ajzen 1980, 1988; Fishbein and Ajzen, 1981), which theorized that actions can be predicted by intentions. Later, Krueger et al. (2000) proposed the competing Shapero-Krueger Model, which links the intentions to exploit an entrepreneurial opportunity to the perceived desirability and perceived feasibility or practicality of the business outcome.[1] On reviewing the empirical evidence of numerous studies, Krueger concluded that both models were validated, but that their model was more robust. For our purposes, the Shapero-Krueger Model has the advantage of focusing on the business decision-maker.

Krueger et al. (2000) have specified the key determinants of perceived desirability and feasibility. First, owner-managers view growth as desirable when the expected outcomes of growth help them meet their personal and business objectives. Thus, expected outcomes are anchored in their motivation for expanding their firm. Second, owner-managers perceive the feasibility of business growth in relation to their self-efficacy; that is, in terms of the business skills they believe they need and have to manage growth. This approach is consistent with the expectancy theory that links work effort and performance to perceptions (Vroom 1964).

The Shapero-Krueger Model describes the cognitive process that leads to growth intentions, but ignores a number of moderating variables that are likely to influence growth intentions, such as resources and opportunities (Wiklund 2001; McKelvie and Chandler 2002), industry structure and business strategy (Chrisman et al. 1998; Minniti 2001). With limited resources in a capital-intensive industry, such as manufacturing, growth intentions are likely to be suppressed. With more resources in an industry requiring a low level of investment, such as consumer services, growth intentions are likely to be enhanced.

## Classification of Young Microfirms

Based on his survey findings, Fillis (2002) proposed a classification of owner-managers of craft microenterprises to help explain their likelihood of growth by becoming international in scope. This classification scheme is specific to craft enterprises where the technical/artistic skills of the operators are critical to the success of the enterprise. However, it can be argued that the classification has wide application in that all microenterprises at the early stages of development share this dependence on the skills of the owner-manager. We therefore propose the following adapted categories of owners: Lifestyler, Entrepreneur, Manager, and Mover (see Figure 1).

This classification scheme (Figure 2) includes a firm characteristic (actual employment: no employees v. some employees) and an owner characteristic (intentions to add employees: no v. yes). At this early stage of firm development, the owner-operator and the firm are closely aligned and intertwined. The Lifestyler is the one-person enterprise, the typical consultant who operates alone and sells his or her expertise. The Lifestyler works alone and has no intention of employing others. In contrast, the Entrepreneur currently works alone out of necessity, but plans to have employees in the near future as the young enterprise becomes more established. On the other hand, the Manager has succeeded in having employees, but has no intention of adding any more, being content with the current size of the enterprise. The market Mover also has succeeded in creating employment, and wants to increase the growth momentum by adding more employees. The Mover has a growth-oriented vision of the enterprise.

| | | Current Employment | |
|---|---|---|---|
| | | **No Employees** | **Some Employees** |
| **Employment Intentions** | **No growth in employment** | Lifestyler | Manager |
| | **Growth in employment** | Entrepreneur | Mover |

**Figure 1. Classification of Young Microenterprises**

| | |
|---|---|
| **Lifestyler**<br>• No employees and no intentions of having any<br>• Concentrates on business services<br>• Low level of sales and investment<br>• Home-based<br>• Desires little growth and sees it as less doable | **Manager**<br>• Employees but no intentions of adding any<br>• Present in all industries<br>• High level of sales and investment<br>• Some leased space<br>• Desires some growth and sees it as moderately doable |
| **Entrepreneur**<br>• No employees but intends on having some<br>• Present in all industries<br>• Low level of sales and investment<br>• Some leased space<br>• Desires growth and sees it as doable | **Mover**<br>• Employees and intends on adding more<br>• Concentrates on consumer services<br>• Highest level of sales and investment<br>• Considerable leased or owned space<br>• Desires growth and sees it as very doable |

**Figure 2. Profile of Four Types of Young Microenterprises**

Only the Entrepreneur and Mover are expected to exhibit high growth intentions. However, their situations differ: The Entrepreneur must acquire and manage employees for the first time, whereas the Mover acquires additional employees and begins to operate at a higher level of complexity. Movers are likely to have more resources, and can obtain leverage from their current employees. Adding employees to an existing human resource base requires less adjustment than hiring, developing, and managing employees as a first-time event. This transition from the owner-operated firm to the owner-managed firm challenges the entrepreneur to acquire and exercise a broader range of managerial and operational skills (Mount et al. 1993). In addition, the Shapero-Krueger Model predicts that these higher levels of growth intentions should be accompanied by higher levels of perceived desirability and feasibility of growth.

## Research Propositions

The literature review and classification scheme described above lead to four propositions for testing purposes.

**Proposition 1 (P1): The four types of young microenterprises (Lifestyler, Entrepreneur, Manager, and Mover) can be differentiated on the basis of personal, business, and industry characteristics.**

**Proposition 2 (P2): The four types of young microenterprises differ in terms of growth intentions, where the Mover aims for higher employment growth than the Entrepreneur.**

**Proposition 3 (P3): The four types of young microenterprises differ in that the Entrepreneur and Mover have the highest levels for perceived desirability of growth.**

**Proposition 4 (P4): The four types of young microenterprises differ in that the Mover has the highest level of perceived feasibility of growth.**

In the next section, we introduce a business survey that helps to test these propositions, and assess the validity of the classification scheme for young microenterprises.

## Methodology

### *Sample*

A telephone survey took place in the summer of 2003 and was executed by two research assistants who followed a set protocol. A list of 549 young firms was obtained from the economic development agencies of two Canadian cities, Ottawa and Sudbury. The combined sample of these two communities (populations of 750,000 and 150,000, respectively) represents a diverse economic base, including resource-based, retail, government and business services, and high technology industries.

### *Questionnaire*

The questionnaire was divided into two sections: growth intentions and firm characteristics. The key variables were measured on a 0 to 100 scale (Krueger et al. 2000, p. 421–422) as specified in Figure 3.

**Perceived desirability:** "How desirable is it for you to grow your business?"
(0 Not desirable to 100 Completely desirable)

**Perceived feasibility:** "How practical is it for you to grow your business?"
(0 Not practical to 100 Completely practical)

**Growth intentions in terms of number of employees** was tapped by two questions:

- How many employees do you currently have? _____Full-time _____Part-time
- How many employees do you intend to have in three years time, by 2006:
  _____Full-time _____Part-time

**Growth intentions in terms of sales** was tapped with one question:

- What is the annual growth in sales that you intend to have:
  In 2004 ___% In 2005: ___% In 2006: ___%

**Moderating variables of growth intentions:** We have included three moderating variables:

1. *Facility:* From where do you operate your business: home v. owned office/retail space v. leased office/retail space
2. *Investment:* How much money have you invested in your business so far, including all personal and external sources?
3. *Industry Type:* What is the main product or service of the business?

**Figure 3. Key Variables**

Facility and investment were considered indicators of resources dedicated to the business, whereas industry was viewed as the context that determines the specific success factors.

## Results

A total of 119 questionnaires were completed. The response rate was 22 percent (119/549). Fifteen of the completed questionnaires were rejected because the firm was either too young (less than 2 years in operation) or too old (11 or more years). Thus, the final count was 104 usable questionnaires of firms 2–10 years of age. All of the respondents were owners or partners and were actively involved in the enterprise.

Given the number of respondents (104) and the total sample size (549), the results have a confidence interval of +/- 8.66 percent at the 95 percent confidence level. Confidence intervals were calculated using The Survey System version 6.01.

The number of employees and the growth intentions in terms of number of employees were calculated on a Full Time Equivalent (FTE) basis. A part-time employee was equivalent to 50 percent of a full-time employee.

Average intended growth in sales was calculated as the average of the intended growth in sales for 2004, 2005, and 2006.

The firms were divided into four industry groupings based on the NAICS two-digit codes: manufacturing, retail, customer services, and business services. Eight firms composed the manufacturing industry grouping (construction and manufacturing), and were omitted only from the industry analysis because there were insufficient cases to allocate across four cells of the firm classification being tested.

### *Characteristics of Firms*

A profile of the sample and the four types of firms is presented in Table 1. These young firms (mean of 4.3 years of age) operated primarily in business and consumer services, and achieved modest annual sales (less than $500,000). Approximately 70 percent of the respondents indicated an investment of less than $50,000 in their home-based business. For firms with employees, the average number of FTEs was 2.7 ranging from 0.5 (one part-time employee) to 14.

When comparing the four types of firms, several significant differences emerged, as measured by the Chi-Square test. The profile of each type of firm highlights these differences. Given the small respondent sample size and the confidence interval of +/- 8.66 percent at the 95 percent level, the differences between the Lifestylers and Movers are reliable, whereas the other comparisons are less so.

***Lifestyler.*** Most of these firms (70%) offered business services, had attained a low level of annual sales (87% reported less than $100,000), and had invested little in the firm (91% indicated less than $50,000). Not surprisingly, 84 percent were home-based businesses.

***Manager.*** While the majority of these firms (57%) offered business services, a large number (43%) operated in consumer services and retail. These firms had a higher level of sales (44% between $100,000 and $499,999), and a higher level of investment (33% indicated $50,000 to $99,999). While most were home-based businesses, 22 percent had leased space.

***Entrepreneur.*** These firms were distributed across industries, but the majority (56%) were in business services. They had achieved a low level of sales (76% had less than $100,000), and most had invested little in the firm (80% indicated less than $50,000). However, 20 percent had leased space.

***Mover.*** Nearly the majority (49%) were in consumer services, had achieved the highest level of sales (71% reported $100,000 or better), and 32 percent had invested over $100,000 in the venture. Thirty-seven percent had leased space, and another 13 percent owned their office or retail space.

### *Intentions of Growth in Number of FTE[2] Employees by 2006*

The Lifestyler firm had no employees, and did not intend on having any in the next three years. In contrast, the Manager firm had a few employees (Mean =1.44 FTE, S.D. = 0.81), but did not intend on expanding its human resources.

The Entrepreneurial firm had no employees, but intended on adding a few over the next three years (Mean = 1.96 FTE, S.D. = 1.46). In the case of the Mover firm, it had employees (Mean = 2.95, S.D. = 2.85), and proposed to add more (Mean = 3.08, S.D. = 2.84).

A T-test indicated that there was no significant evidence that Mover firms were currently larger than Manager firms (n.s.). Similarly, there was no significant support that Mover firms intended more growth in FTEs than Entrepreneurial firms, though the results were in the expected direction (sig. = .074). Thus, P2 is not supported. These results are understandable given the large standard deviations present in the data subsets.

### *Perceived Desirability and Feasibility of Growth*

Table 2 summarizes the ANOVA tests on the growth-related variables. The types of firms were compared on average intended annual sales growth (%) over the next three years. On average, the respondents indicated an intended growth of 25.5 percent. Though the F statistic was not significant ($p = 0.145$), the mean percentages were in the expected order, with Mover and Entrepreneur firms reporting the higher growth goals (33.1% and 29.8%), and the Lifestyler and Manager the lower sales goals (16.8% and 13.0%).

**Table 1. Profile of Four Types of New Microenterprises**

| | *Sample* | *Lifestyler* | *Manager* | *Entre-preneur* | *Mover* | *Chi-square* | |
|---|---|---|---|---|---|---|---|
| FTEs (0 = no, 1 = yes) | | 0 | 1 | 0 | 1 | | p |
| Intended Growth in FTE | | | | | | Value | (2 sided) |
| 0 = no growth, 1 = growth | | 0 | 0 | 1 | 1 | | |
| Number of cases | 104 | 31% | 9% | 24% | 37% | | |
| Average age of business, yrs | 4.32 | 4.66 | 3.56 | 4.48 | 4.11 | | |
| Average number of FTEs | | | 1.44 | | 2.95 | | |
| Average intended growth in FTEs | | | | 1.96 | 3.08 | | |
| **Industry grouping**[a] | | | | | | | |
| retail | 14% | 3% | 14% | 16% | 23% | | |
| business services | 51% | 70% | 57% | 56% | 29% | | |
| consumer services | 35% | 27% | 29% | 28% | 49% | 12.99 | 0.043 |
| **Sales for past year** | | | | | | | |
| less than $100,000 | 61% | 87% | 56% | 76% | 29% | | |
| $100,000 to $499,999 | 37% | 13% | 44% | 20% | 66% | | |
| $500,000 + | 3% | 0% | 0% | 4% | 5% | 33.7 | 0.000 |
| **Investment** | | | | | | | |
| less than $10,000 | 28% | 44% | 44% | 32% | 8% | | |
| $10,000 to $49,999 | 42% | 47% | 22% | 48% | 39% | | |
| $50,000 to $99,999 | 16% | 6% | 33% | 16% | 21% | | |
| $100,000 + | 13% | 3% | 0% | 4% | 32% | 29.4 | 0.001 |
| **Facility** | | | | | | | |
| home | 67% | 84% | 78% | 76% | 45% | | |
| owned office/retail space | 6% | 0% | 0% | 4% | 13% | | |
| leased office/retail space | 22% | 6% | 22% | 20% | 37% | | |
| other | 5% | 9% | 0% | 0% | 5% | 21.2 | 0.012 |

[a] N= 96. Eight firms composed the manufacturing industry grouping (construction and manufacturing), and were omitted from the industry analysis.

As for desirability of growing the business (scale of 0 to 100), there were significant differences among the types of firms (p = 0.000): The Mover and the Entrepreneur indicated higher levels of desirability (87.3 and 72.2) than the Manager and Lifestyler (64.4 and 54.2). Thus, P3 is supported. Similarly, there were significant differences in terms of the practicality of growing the business (p = 0.000): The Mover reported the highest level of readiness to grow (82.5), followed by the Entrepreneur and the Manager (69.6 and 68.9), and finally by the Lifestyler (52.5). Thus, P4 is supported.

### *Limitations of the Study*

This study is based on a convenience sample. As such, it suffers from a number of design weaknesses. The sample is tied to a client mailing list prepared by two economic development corporations and not to a census of the businesses in the two communities. The mailing list contained only the name of the company and the contact person; no information was available that would allow for a comparison between the mailing list and the responding sample. Furthermore, the response rate was relatively low, which

**Table 2. ANOVA on Desirability and Practicality of Growing the Business**

| | *Sample* | *Lifestyler* | *Manager* | *Entre-preneur* | *Mover* | *ANOVA F* | *p* |
|---|---|---|---|---|---|---|---|
| | n=104 | n=32 | n=9 | n=25 | n=38 | | |
| Average intended annual sales growth next 3 yrs, % | 25.54 | 16.77 | 12.96 | 29.84 | 33.09 | 1.839 | 0.145 |
| **Desirability of growing business** | | | | | | | |
| mean | 71.53 | 54.22 | 64.44 | 72.2 | 87.34 | 9.914 | 0.000 |
| standard deviation | 28.78 | 30.35 | 28.77 | 26.54 | 19.22 | | |
| **Practicality of growing business** | | | | | | | |
| mean | 68.99 | 52.5 | 68.89 | 69.6 | 82.5 | 8.289 | 0.000 |
| standard deviation | 27.62 | 29.13 | 26.14 | 30.45 | 15.49 | | |

scale of 0 (not desirable/practical) to 100 (completely desirable/practical)

impacts the reliability of the findings as indicated by the large confidence intervals. Given these inherent weaknesses, the reader is advised to consider cautiously the findings for reflection instead of prediction. Despite these limitations, the study is considered valuable because it focuses on small young enterprises that often elude robust business studies.

As stated above, it was impossible to compare the characteristics of the responding sample (n = 104) to those of the survey sample (n = 549). However, as expected, the responding sample was composed of young firms from a variety of industries, with a range of both sales and investment levels and a variety of business facilities. Though our findings are limited to the responding sample, they remain a valuable guide for agencies that serve a diversified economic base.

Our sample of young firms included only those that approached an economic development agency for services. Therefore, the sample excluded young firms that chose not to contact such an agency. Our findings are useful for these agencies as they attempt to improve the support services they offer to their traditional clients, but less so to their non-traditional clients. Our sample may also have excluded microfirms operating along new business models.

Future research is required to confirm our findings because this study suffers from weaknesses in reliability and validity due to the small convenience sample used and the resulting confidence interval of +/- 8.66 percent at the 95 percent level for the statistics generated. In other words, our findings can be challenged and considered unrepresentative and inaccurate. It is recommended that the research design be expanded to include before–after measures to capture the impact of intentions over time and the entrepreneurial activities that make growth possible. We expect that the entrepreneurial behaviors are varied (Carter et al. 1996) and focused on building the business and dealing with the business environment. The questionnaire would be administered twice, once to measure the initial condition of the firm and the growth intentions, and the second time to record the entrepreneurial behaviors that have taken place and measure the actual growth that has occurred. The study would span one year of business activity—sufficient time for change to happen but not so long that the researcher loses contact with the respondents. Within this time series design, subjects act as their own controls. However, to reduce the risk of extraneous factors influencing the outcomes, the researcher should keep a historical record of significant local events that may have some impact on economic climate and business activity. Finally, a large stratified random sample including all industries would be appropriate and reflect a business census of the city or region targeted.

## Discussion

The survey findings support the proposition (P1) that the four types of young microenterprises (Lifestyler, Entrepreneur, Manager, and Mover) can be differentiated on the basis of personal, business, and industry characteristics. From the economic development goal of creating jobs, it would be appropriate to tailor an approach for each type of firm.

The Lifestyler needs no or little assistance because the objective of the Lifestyler is self-employment and nothing more. The Entrepreneur shows desire of growing the business but so far has been unable to create employment. The entrepreneur is committed, but may need assistance to make growth feasible. In contrast, the Manager shows promise only on the basis of business characteristics: the firm has achieved some level of success and has employees. In this case, the main impediment to employment growth is the lack of a business vision including growth. Agency staff could help, but would need to persuade these Managers that their current view of their firm is unduly limiting, and perhaps disadvantageous in a changing business environment.

The Mover is the star in that these firms have successfully grown, and the businessowners intend to expand the workforce. The likelihood of creating more jobs is high. In so far as they concentrate on consumer services, agency staff could advise them on the success factors of this industry sector, and explore exporting possibilities.

Interestingly, although Movers had higher intended average annual sales growth compared to the others, all the firms intended to increase their annual sales by a substantial amount, whether they had employees or not. Obviously, they viewed growth in sales as much easier to accomplish, even with limited resources. The decision to hire an initial employee, or add employees, commits the owner to financial obligations and forces new ways of running the business to ensure a productive workforce, and many were not willing or ready to do that.

Agency staff must rely on their training and experience to guide the businessowners in creating, implementing, and sustaining a growth strategy. However, engaging these small businessowners in a meaningful manner involves practical solutions for the ongoing operation of their business. In other words, a growth vision and strategy must be concrete, and any agency intervention should be based on experiential learning (Deakins and Freel 1998) and user-friendly learning strategies such as those outlined by Dyer and Ross (2004):

1. Encourage more awareness, self-reflection, and self-examination.
2. Involve others in a dialogue and thus act as mentors and coaches.
3. Formalize the process of business planning with learning-oriented computer programs.

Cope and Watts (2000) also recommended the use of mentors who would have a detailed knowledge of both the owners and the businesses, and could create the constructive context for both reflection and action.

For firms with employees, or with intentions of adding employees, the issues of training and delegation of duties become very important. We can assume that the businessowner assesses whether each employee has the requisite skills, and whether the skill gaps require some kind of remedial action (training to upskill or job simplification to downskill). However, only skillful employees create the foundation for delegation and teamwork—hallmarks of the growing firm. The business advisor or mentor can help to raise the level of awareness among businessowners on these issues through an ongoing dialogue.

In a survey of young firms, Ardichvili et al. (1998) reported that accounting was the first function to be delegated and the only area in which outside experts played a significant operational role. Growth in employee numbers was accompanied by increased delegation of a number of functional activities. The greater the number of full-time employees added (1 or less versus 2–8), the higher the level of delegated activities in production and service delivery, including purchasing and computer systems. They recommended structured training for employees in all of these areas at the same time. In the case of rapid growth (9+ employees), sales and marketing-related activities were likely to be delegated to either employees or new managers. While employees would benefit from structured training, new managers can be hired from the outside who come with strong competencies in marketing and sales. This advice appears relevant to the Movers who resemble the sample of young firms in Ardichvili et al. and less relevant to the Entrepreneurs who are having employees for the first time and are likely to retain close involvement in all of the firm's activities. Persuading the Movers that their employees need training on a wide front will meet with resistance on the basis of costs and preference for on-the-job training.

As for business planning, Ardichvili et al. (1998) reported that, irrespective of growth in number of employees, the original management team continued to be closely involved in this "strategic" activity. They recommended executive development focused on strategic decision making and on understanding the competitive and wider environment. This advice appears to hold for the Entrepreneurs, Movers, and Managers; however the latter are likely to have low awareness of such a need and to question the benefits. In any case, delivery of this executive development would have to be low cost and flexible.

Ardichvili et al. (1998) reported that functional delegation appeared to be similar for manufacturing and service firms when annual sales were less than $10 million. In their opinion, their training and development recommendations did not require tailoring to industry-specific contexts. That being said, the owner-managers will want a tailored-service that reflects the young firm's "unique" situation.

Delegation is a multistep process that includes job design, selecting the right person, and implementing the new working relationship. A mentor would be in a position to guide the owner through this complex process that is situated within the particular context of that owner and that business.

## Conclusions

In the pursuit of employment growth, business support agencies are well advised to distinguish among the four types of young microfirms so that their assistance and interventions be as effective as possible. To focus resources on the young firms that are likely to experience strong employment growth, the agencies should prioritize as follows:

1. Movers deserve the most attention because both the personal and business characteristics are favorable for employment growth.
2. Entrepreneurs and Managers deserve some attention because either the personal or business characteristics (but not both) are favorable for employment growth
3. Lifestylers do not merit any special effort beyond the standard services because all of the key characteristics oppose employment growth.

Solicitation and assistance would have to be tailored to match the particular context of each type of firm.

## Acknowledgment

The authors are grateful for the comments and suggestions of two anonymous reviewers and for statistical advice from Dr. Rashmi Garg of the Psychology Department at Laurentian University.

## Endnotes

1. The model includes a third variable: propensity to act. The variable is excluded here because Krueger et al. (2000) found that it added little explanatory power.
2. FTE was calculated as number of full-time employees plus 50 percent of the number of part-time employees.

## References

Ardichvili, A., R. Cardozo, P. Reynolds, and M. Williams. 1998. The new venture growth: Functional differentiation and the need for human resource development interventions. *Human Resource Development Quarterly* 9,1: 55–70.

Autio, E., R. Keeley, M. Klofsten, and T. Ulfstedt. 1997. Entrepreneurial intent among students: Testing an intent model in Asia, Scandinavia and in the USA. *Frontiers of Entrepreneurship Research.* Wellesley, MA: Babson College, 133–147.

Ajzen, I. 1980. *Understanding attitudes and predicting social behaviour.* Englewood Cliffs: Prentice-Hall.

Ajzen, I. 1988. *Attitudes, personality, and behaviour.* Open University Educational Enterprises Limited.

Armitage, C., and M. Conner. 2001. Efficacy of the theory of planned behaviour: A meta-analytic review. *British Journal of Social Psychology* 40,4: 471–499.

Birch, D., A. Gundersen, and W. Parsons. 1999. *Corporate demographics,* Cambridge, MA: Cognetics Inc.

Bird, B. 1992. The operation of intentions in time: The emergence of the new venture. *Entrepreneurship Theory and Practice* 17,1: 11–27.

Bird, B. 1988. Implementing entrepreneurial ideas: The case for intention. *Academy of Management Review* 13,3: 442–453.

Carter, N., W. Gartner, and P. Reynolds. 1996. Exploring start-up event sequences. *Journal of Business Venturing* 11: 151–166.

Chaganti, Radha, Ronald G. Cook, and Wayne J. Smeltz. 2002. Effects of styles, strategies, and systems on the growth of small businesses. *Journal of Developmental Entrepreneurship* 7,2: 175–192.

Chrisman, James J., Alan Bauerschmidt, and Charles W. Hofer. 1998. The determinants of new venture performance: An extended model. *Entrepreneurship Theory and Practice* 23,1: 5–29.

Cope, Jason, and Gerald Watts. 2000. Learning by doing—A exploration of experience, critical incidents and reflection in entrepreneurial learning. *International Journal of Entrepreneurial Behaviour & Research* 6,3: 104–124.

Deakins, D., and M. Freel. 1998. Entrepreneurial learning and the growth process in SMEs. *The Learning Organization* 5,3: 144–155.

Dennis, W., and G. Solomon. 2001. Changes in the intention to grow over time. *Frontiers of Entrepreneurship Research.* Wellesley, MA: Babson College.

Doll, J., and I. Ajzen. 1992. Accessibility and stability of predictors in theory of planned behavior. *Journal of Personality and Social Psychology* 63,5: 754–756.

Dyer, L., and C. Ross. 2004. Learning from experience in the small business: Potential pitfalls in the process. *Proceedings of the Conference of the Administrative Sciences Association of Canada,* Ed. T. Menzies. Quebec, Que.: ASAC, CD-ROM version.

Feldman, Daniel, and Mark Bolino. 2000. Career patterns of the self-employed: Career motivations and career outcomes. *Journal of Small Business Management:* 53–67.

Fillis, Ian. 2002. The internationalization process of the craft microenterprise. *Journal of Developmental Entrepreneurship* 7,1: 25–43.

Fishbein, M., and I. Ajzen. 1981. On construct validity: A critique of Miniard and Cohen's paper. *Journal of Social Psychology* 17: 340–350.

Halabisky, D., E. Dreessen, and C. Parsley. 2004. Growth firms in Canada, 1985–1999. *Proceedings of the Conference of the Administrative Sciences Association of Canada,* Ed. T. Menzies. Quebec, Que.: ASAC, CD-ROM version.

Industry Canada. May 2003. *Key small business statistics.* www.strategis.gc.ca/sbstatistics.

Industry Canada. 2002. Small Business Research and Policy Web Site, Statistics Section. Small Business Policy Branch, Policy Research Group, Version 7.2.

Industry Canada. 1996. *Small business in Canada: A statistical overview*.

Kim, M. S., and J. E. Hunter. 1993. Attitude-behavior relations: A meta-analysis. *Journal of Communication* 43,1: 101–142.

Krueger, N., M. Reilly, and A. Carsrud. 2000. Competing models of entrepreneurial intentions. *Journal of Business Venturing* 15: 411–432.

McKelvie, A., and G. Chandler. 2002. Patterns of new venture development. *Frontiers of Entrepreneurship Research.* Abstract. Wellesley, MA: Babson College.

Morrison, Alison, John, Breen, and Shameen Ali. 2003. Small business growth: Intention, ability and opportunity. *Journal of Small Business Management* 41,4: 417–425.

Minniti, M. 2001. Self-employment and organization creation: The case of Italy. *Frontiers of Entrepreneurship Research.* Abstract. Wellesley, MA: Babson College.

Mount, J., J. T. Zinger, and G. Forsyth. 1993. Organizing for development in the small business. *Long Range Planning* 26,5: 111–120.

OECD. 2000. *High growth SMEs: Phase II synthesis report.*

Orser, B., S. Hogarth-Scott, and P. Wright. 1998. On the growth of small enterprises: The role of intentions, gender and experience. *Frontiers of Entrepreneurship Research.* Wellesley, MA: Babson College, 366–380.

Reitan, B. 1996. Entrepreneurial intentions—A combined models approach. Paper presented at the 9th Nordic Small Business Research Conference, Lillehammer, Norway.

Rumball, D. 2001. *The dynamics of growth: Is high growth sustainable?* Prepared for the Government of Ontario, Canada, and available at: http://www.ontariocanada.com/ontcan/en/PDF_HTML/Priority-2/w-e-dynamics-of-growth.htm.

Rutherford, Matthew, Patrick McMullen, and Sharon Oswald. 2001. Examining the issue of size and the small business: A self-organizing map approach. *Journal of Business and Economic Studies* 7,2: 64–81.

Stanworth, Celia and John Stanworth. 1995. The self-employed without employees—Autonomous or atypical? *Industrial Relations Journal* 26,3: 221–230.

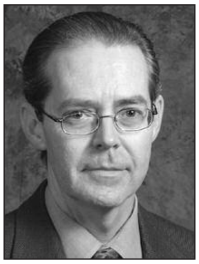
Vroom, V. H. 1964. *Work and motivation.* New York: Wiley.

White, K. 2002. *High-growth companies—Mapping Canada's entrepreneurial landscape.* Industrial Analysis and Strategies Branch, Industry Sector, Industry Canada.

Wiklund, J. 2001. Growth motivation and its influence on subsequent growth. Frontiers of Entrepreneurship Research. Abstract. Wellesley, MA: Babson College.

Wiklund, J., P. Davidsson, F. Delmar, and M. Aronsson. 1997. Expected consequences of growth and their effect on growth willingness in different samples of small firms. Frontiers of Entrepreneurship Research. Wellesley, MA: Babson College, 1–16.

## About the Authors



**Rolland LeBrasseur** (rlebrasseur@laurentian.ca) is a professor of organizational behavior on the Faculty of Commerce and Administration at Laurentian University, and chair of the Small Business Research Group. He is a member of the Editorial Review Board of the *Journal of Small Business & Entrepreneurship.* Dr. LeBrasseur's current interests include survival and failure of business start-ups, initial growth of firms, and intelligent communities.

**Huguette Blanco** (hblanco@laurentian.ca) is professor of accounting at Laurentian University, Faculty of Commerce and Administration. Dr. Blanco has published and made conference and seminar presentations in the areas of small business management, economic development, and the management of safety.

**John L. Dodge** (jdodge@laurentian.ca) is a professor of strategic management and e-business within Laurentian University's Faculty of Commerce and Administration and is director of e-business science at the university. His current interests include SME development and technology adoption.

# A Cross-Country Assessment of Government Intervention and Entrepreneurial Activity

Maria Minniti

*Recent studies have shown that the contribution of small firms to employment and GDP is increasing. A large amount of work has also established the significance of social and economic variables for entrepreneurial decisions. Very little is known, however, about how government policies and programs influence entrepreneurial activity, and whether these effects are consistent across countries. Using original data from a representative sample of 10,000 individuals and from more than 300 open-ended interviews in 10 countries, this article provides some suggestive evidence that government intervention aimed at enhancing the underlying environment of entrepreneurial decisions may be more effective than intervention designed to provide safety nets.*

In recent years, several studies have provided significant evidence on the ability of smaller and entrepreneurial firms to create employment and contribute to economic development and growth (Acs et al. 1999; Baumol 2002; Birch 1987). New and small firms constitute more than 99 percent of all firms in almost all advanced countries, and their share of employment and contribution to the Gross Domestic Product is increasing (OECD 1996; Carree and Thurik 2003). Acs et al. (1999) and Wennekers and Thurik (1999), among others, have shown that, in recent years, the role played by entrepreneurship in productivity and GDP growth has expanded significantly. In fact, entrepreneurship is now acknowledged as a major source of economic growth and many governments and international organizations have launched initiatives for the support and development of the entrepreneurial sector.[1]

Within this context, a sizable amount of empirical work has established the significance of both social and economic variables in determining entrepreneurial decisions. Among others, Evans and Jovanovic (1989), Evans and Leighton (1989), and Kihlstrom and Laffont (1979) have discussed the importance of financial resources and constraints on entrepreneurial decisions. Iyigun and Owen (1998), Murphy et al. (1991), and Otani (1996) have discussed issues related to the allocation of human capital. Bogenhold and Staber (1991), Blanchflower and Oswald (1988), and Hamilton (2000) have studied the importance of employment status and labor markets on entrepreneurial decisions. Finally, Amit et al. (1995) have focused on individuals' opportunity costs when choosing between alternative income-producing activities. The complementarities between many of these works have drawn attention to the fact that entrepreneurial decisions are the outcome of a multilayered and complex process and that understanding the sequence of actions required to start a new firm is, to a large extent, contingent upon the context in which they are taken (Jacks and Anderson 2002).

Very few studies, however, have tried to establish how, if at all, government policies and programs influence the level of entrepreneurial activity. Some significant exceptions are Brenner (1987), Holcombe (2003), Maggioni et al. (1999), Porter (1990), Spencer et al. (2005), and Wren and Storey (2002). In 1990, Porter argued that a nation's competitiveness depends on the capacity of its industry to innovate and upgrade. By focusing on innovation, he indirectly brought attention to the importance of the entrepreneurial sector on economic growth and to the possible role of the government in fostering entrepreneurship. Brenner (1987) posed more precisely the broad issue of the role of the statesman with respect to entrepreneurship policy. In his view, entrepreneurial ventures are often the outcome of a desire to overcome adverse social or economic handicaps. Thus, he argued, policy-makers need to encourage free trade while, at the same time, recognize the concerns of those in danger of being left behind. Along complementary lines, and building on Kirzner (1973), Holcombe (2003) provided a taxonomy of the origins of entrepreneurial opportunities, including factors that disequilibrate the market and factors that enhance production possibilities. His line of reasoning led directly to policy implications regarding the economic environment more conducive to entrepreneurial discovery and to the role of government in research and development. Spencer et al. (2005), instead, suggested the existence of a relationship between a government's interest in the maximization of power and its willingness to support the creation of new industries. At a more applied level of analysis, using the case of Italy, Maggioni et al. (1999) evaluated the impact of public entrepreneurial policies on the postentry performance of new businesses and showed the existence of mixed effects. In fact, government aid was shown to allow firms to have higher levels of technology. However, the same government aid was also found to support inefficient firms. Finally, using the UK example, Wren and Storey (2002) assessed the impact of publicly provided soft subsidies on the performance of small and medium enterprises. They found no effect on smaller firms but a positive and significant effect on survival rates and growth rates for mid-range SMEs.

Overall, although some studies exist on the effects of government policy on entrepreneurship, very little has been done to determine whether these effects are consistent across countries. The relative lack of comparative studies on the implications of policy action for entrepreneurs is due, at least in part, to the paucity of reliable information and, in particular, to the difficulty of obtaining relevant data. The purpose of this article is to contribute to the elimination of this gap by providing some initial answers on this important question. Specifically, the article discusses the extent to which government policies, such as those concerning taxes, regulations, and procurements, are either size-neutral or encourage new and growing firms. In addition, the article tries to assess the effectiveness of government programs and initiatives aimed at directly assisting new and growing firms. The article's overall goal is to generate discussion and further research on the role played by government on entrepreneurial activity by showing that, although, entrepreneurial policies need to be fitted to their local context, it appears that cross-cultural (universal) phenomena are also at play and should be taken into account by policy-makers.

Government policies and programs mold institutional structures for entrepreneurial action, encouraging some activities and discouraging others (Dobbin and Dowd 1997). Public policy shapes the rules of competition and creates niches where investment and entrepreneurial activities are perceived as being more or less attractive (Boettke 1993; Boettke and Coyne 2003). Finally, the nature of political interventions influences alertness (Harper 1998). Thus, policies and programs that improve transparency and entitlement tend to increase the subjective perception of the link between actions and outcome. Harper, for example, argued that "an environment of freedom is more likely than other environments to generate internal locus of control beliefs and acute entrepreneurial alertness" (1998, p. 253).

Furthermore, government policy and programs also influence the fate of organizations by disrupting established ties between firms and resources (Carroll et al. 1988; Stinchcombe 1965). Baumol (1990) argued that institutional arrangements affect the quantity and type of entrepreneurial efforts and that ". . . the exercise of entrepreneurship can sometimes be unproductive or even destructive, and that whether it takes one of these directions or one that is more benign depends heavily on the structure of payoffs in the economy—the rules of the game" (Baumol 1990, p. 899). In general, government policies and programs may be crucial in determining the quantity and quality of entrepreneurial behavior as they define the incentives for individuals to transform perceived opportunities into actions and contribute to determining the extent to which the environment is supportive of and conducive to entrepreneurial behavior.

The overriding goal of this article is to provide some initial cross-country evidence of the role played by government in shaping entrepreneurial behavior and, hopefully, to initiate a much needed debate on best and worst practices and on the general ability of governments to influence entrepreneurial behavior.

## Variables and Data

Data used in this study are from the Global Entrepreneurship Monitor (GEM) project. Started in 1999, the GEM project is an ongoing, large-scale international study designed to understand the relationship between entrepreneurship and economic activity.[2] All data used in this article are original and were collected simultaneously with standardized procedures during winter 1999 in Canada, Denmark, Finland, France, Germany, Italy, Israel, Japan, United Kingdom, and United States. The 10 countries in the sample share several relevant social and economic characteristics.[3] Differences across their entrepreneurship rates may be attributed, to some extent, to factors other than socioeconomic circumstances. As a result, the selected countries provide a good sample for studying the influence that variables, such as government policy and programs, have on entrepreneurial activity.

The timing of the data collection is not relevant for the argument in the article. The point of this research is neither to evaluate any particular policy nor to propose benchmarking or best practices. Also, the evidence emerging from the 10 countries considered here is suggestive, and the article contains no attempt to generalize these results to other countries or to compare the relative performances of different groups of countries. This article presents a discussion, and its goal is to initiate a debate about the ability of governments to influence (positively or negatively) entrepreneurial behavior.

The GEM project includes the collection of three types of data. First, a survey is administered simultaneously in each country to a representative stratified random sample of the population. In 1999, surveys were stratified geographically and household sample selection was based on random direct dialing or using listed numbers. All surveys were conducted by phone, except in Japan were they were conducted face to face. Also, in 1999, the sample size was of at least 1,000 people per country for a total of 10,422 individuals.[4] In the survey, entrepreneurship is defined as: "Any attempt at new business or new venture creation, such as self-employment, a new business organization, or the expansion of an existing business, by an individual, a team of individuals, or an established business (Reynolds et al. 1999, p.3)."[5] Although this definition does not allow for a clear distinction between entrepreneurial behavior motivated by growth strategies and entrepreneurial behavior motivated by self-sufficiency, still it has a wide range of applicability and is consistent with well-established literature on the subject (e.g., Gartner 1985, 1990). An interesting feature of the GEM dataset is that it does not focus, as most studies do, on the existing number of small firms or on firm birth and death rates. Rather, GEM data capture the entrepreneurial mindset of individuals in different countries. In this sense, the data are very suitable for the study of how policies and programs influence individuals' decisions since they are not affected by hindsight or survival biases.

Items in the survey focused primarily on providing an estimate of the percentage of the adult population (18–64 years of age) actively involved in starting a business. In each of the 10 countries, adults participating in the survey were asked a series of questions about their involvement in entrepreneurial activities, including whether they were currently starting a firm on their own or on behalf of their employer as part of their job. Those who responded yes to either or both questions were considered nascent entrepreneurs if, in addition, they were also expecting to own part of the new firm and if the initiative was not an operating business at the time of the interview. Figure 1 provides a detailed description of questions and procedures used by GEM to classify respondents as being involved in entrepreneurial activity.[6]

In addition to the survey, in each country, GEM researchers conducted face-to-face interviews to gain information about nine preselected factors. The list of nine factors was compiled on the basis of existing literature that had shown their relative importance for entrepreneurial decisions. The list of constructs included:

1. *Government policies:* The extent to which government policies reflected in taxes, regulations, procurements, or the application of any are either size-neutral or encourage new and growing firms.
2. *Government programs:* The presence of programs and initiatives to assist directly new and growing firms at all levels of government (national, regional, municipal).
3. *Financial support:* The availability of financial resources, equity, and debt, for new and growing firms including grants, collateral, and subsidies.
4. *Education and training:* The extent to which training in creating or managing small, new, or growing business is incorporated within the educational and training systems at all levels.
5. *Research and development transfers:* The extent to which national research and development will lead to new commercial opportunities and whether these are available for new, small, and growing firms.
6. *Commercial and professional infrastructure:* The presence of commercial, accounting, and other legal services and institutions that encourage and support the emergence of new, small, or growing businesses.
7. *Internal market openness:* The extent to which commercial arrangements undergo constant change and redeployment as new and growing firms compete and replace existing suppliers, subcontractors, and consultants.
8. *Access to physical infrastructure:* Ease of access to available physical resources (communication, utilities, transportation, land, or space) at a price that does not discriminate against new, small, or growing firms.
9. *Cultural and social norms:* The extent to which existing social and cultural norms encourage, or do not discourage, individual actions that may lead to new ways of conducting business or economic activities and may, in turn, lead to greater dispersion in personal wealth and income.

Relevant literature addressing the role played by *government policy* and *programs* has been discussed in the introduction to this article. Within this context, however, it is worth recalling that although most scholars now agree that governments have the ability to influence the entrepreneurial sector, no general agreement exists yet on exactly what this role ought to be and whether a proactive and specific approach to entrepreneurial policy ought to be preferred. Investigating this issue is the goal of this article. With respect to *financial support,* Audretsch and Elston (2002), Evans and Jovanovic (1989), Hamilton (2000), and Kihlstrom and Laffont (1979) are just a few examples of works that have discussed the importance of financial resources and constraints on entrepreneurial decisions. Overall, they have shown that entrepreneurs are constrained by lack of resources and that a positive correlation exists between an individual's wealth and income and his probability of getting involved in starting a business. The importance of *education and training* for entrepreneurial decision has been the object of much debate in light of the increasing number of programs focusing on entrepreneurship education. In general, the relationship between education and new firm formation is uncertain, except for richer countries where post graduate training has been shown to have some positive effects on high-tech start-up rates (Blanchflower 2004).

Because of the increasing importance of high-tech start-ups, *research and development transfers* have been the subject of several studies (Degroof and Roberts 2004; Markman et al. 2005; Peters et al. 2004). Overall, this literature has established the importance of incubators, university patenting, and spin-off activities, as well as investigated the role played by alternative arrangements with respect to property rights and their effect on entrepreneurial incentives. Less work has been devoted, instead, to studying the importance of *commercial and professional infrastructure* and of *access to physical infrastructure.* Van de ven (1993) and Venkataraman (2004) emphasized the importance of

*All respondents were asked three basic questions:*

1a. Are you, alone or with others, currently trying to start a new business, including any type of self-employment? (yes, no, don't know, refuse)
1b. Are you, alone or with others, trying to start a new business or a new venture with your employer—an effort that is part of your normal work? (yes, no, don't know, refuse)
1c. Are you, alone or with others, the owner of a company you help manage? (yes, no, don't know, refuse)

***Nascent Entrepreneurs***
*Respondents who answered "yes" to items 1a or 1b, were then asked:*

2a. You mentioned that you are trying to start a new business. Over the past 12 months have you done anything to help start this new business, such as looking for equipment or a location, organizing a start-up team, working on a business plan, beginning to save money, or any other activity that would help launch a business? (yes, no, don't know, refuse)
2b. Will you personally own all, part, or none of this business? (all, part, none, don't know, refuse)
2c. Has the new business paid any salaries, wages, or payments in kind, including your own, for more than three months? (yes, no, don't know, refused)

Respondents were coded as "nascent entrepreneur" if, in addition to 1a and 1b, they answered "yes" to 2a and 2b, and "no" to 2c.

***New Businessowners***
*To make the distinction between individuals involved in starting a new business (nascent entrepreneurs) and those involved in managing a very young business (baby businessowners), respondents who answered "yes" to question 1c were asked:*

3a. You said you were the owner or manager of a company. Do you personally own all, part, or none of this business? (all, part, none, don't know, refuse)
3b. What was the first year the owners received wages, profits, or payments in kind? (4-digit year, or no profits yet, don't know, refuse)

*Respondents who classify as full or part owners of the business and had received wages or salaries paid up to 42 months were coded as "baby business owners."*

**Figure 1. Questions and Procedures Used to Classify Respondents**

sound legal systems, transparent capital markets, advanced transportation and telecommunications, etc. Venkataraman (2004) also emphasized the importance of *internal market openness* as one of the conditions necessary for government intervention to produce tangible results. Due to the high level of development of all countries included in the sample, market openness and quality of infrastructure turned out to be less important than the other constructs. Most likely, the results with respect to those variables would have been significantly different with a group of developing countries.

Finally, a growing body of literature has established the importance of *cultural and social norms* for entrepreneurial behavior. In addition to the embedded nature of much entrepreneurship (Jacks and Anderson 2002), and building on Hofstede's conceptualization of national culture, these works have shown that the level of economic development, culture, and institutions all influence the demand for entrepreneurship by creating opportunities available for start-ups. In addition, these works suggested that cultural and institutional conditions have an impact on the supply of entrepreneurship because of their ability to influence the skills, resources, and preferences of individuals within the population (Hayton et al. 2002; Frederking 2004).

Between 35 and 50 open-ended, standardized face-to-face interviews were conducted in each country (at least three individuals per country for each of the nine constructs listed above) for a total of 338 interviews across the 10 countries in the sample. Interviewed individuals, called *key informants,* were entrepreneurship experts selected among academics, government officials, venture capitalists, and other well-known individuals with significant expertise in one of the nine areas listed above. In each country, a special effort was also made to select key informants so as to represent geographical, ethnical, and gender differences adequately.[7] During the interviews, each informant was asked to identify and discuss the factor he or she considered to be most relevant for the future of entrepreneurship in that country. The selected factor, called the *main issue,* identified the dominant issue influencing entrepreneurial decisions in that country at the time of the interview according to the person interviewed. In addition to the main issue, each key informant was asked to select at least three *discussion issues;* that is three factors he or she considered to be particularly relevant, though not dominant, for the future of entrepreneurship in that country from the list of nine pre-selected factors.[8] Responses from the key informants allowed an initial assessment of the relative importance, in each country and across countries, of each of the nine selected factors.

Finally, at the end of the interview, each key informant was given a 10-page questionnaire from which the third type of data was obtained. In addition to demographic information, questionnaires contained a minimum of five questions for each of the nine preselected factors. Each question was presented as a standardized fixed-response item. Responses were then combined and used to calculate multiitem indices for each of the nine selected factors.[9] Results presented in this article rely primarily on questionnaires and interview data, while survey data were used only to report entrepreneurial propensity rates in each of the 10 countries. All data used in this article are GEM data and were collected in all countries during the spring and summer of 1999.

## Some Cross-country Evidence on Government Policy and Programs

Data collected through the adult population surveys were used to estimate what percentage of individuals were involved in starting a business in 1999. Raw data were weighted to be representative of the entire population. Table 1 shows that rates of entrepreneurial propensity for each country and the corresponding confidence levels. Such rates varied between countries from 1.4 percent in Finland to 8.4 percent in the United States (Reynolds et al. 1999).[10] The spread in entrepreneurial prevalence rates is quite large, ranging from more than 1 in every 12 individuals in the United States (e.g., 8.4% of the adult population), to less than 1 in every 67 individuals in Finland.

The results above suggest that even across countries with relatively similar socioeconomic environments, such as the 10 countries in the sample, the rates of entrepreneurial propensity differ significantly. But what causes these differences? Data from the key informants' questionnaires were used to construct multiitem indices for each of the nine factors identified as being relevant for entrepreneurial decisions.

For each of the nine factors, and for each country, the values across the relevant five answers on the questionnaires of all key informants were averaged to compute that country's index. The weighted average value of each set of indices across countries was then computed to obtain the cross-country index for that issue. Table 2 shows the correlation between entrepreneurial propensity and the indices representing the nine entrepreneurial factors as well the Chronback Alphas for each index.[11] Favorable cultural and social norms, availability of financial support, and ease of R&D transfers are shown to be positively and significantly correlated with the rates of business start-ups. Access to commercial and professional infrastructure and the existence of relevant education and training are shown to be also somewhat relevant. Correlation is weak or absent, instead, between start-up rates and internal market openness. As mentioned earlier, this result is not surprising since all 10 countries in the sample are relatively well developed and have democratic and stable institutions. In such environments, market openness is often taken for granted and its value underestimated. More surprising, instead, is the very weak correlation between start-up rates and government policies and programs. While Table 2 suggests a low positive correlation between government policy and entrepreneurial propensity, government programs are shown to be virtually uncorrelated to it.

**Table 1. Percentage Rates of Entrepreneurial Propensity by Country (95% Confidence Level)**

| | *Low* | *High* | *Mean* | *SE* |
|---|---|---|---|---|
| Finland | 0.62 | 2.18 | 1.40 | 0.40 |
| Japan | 0.85 | 2.35 | 1.60 | 0.40 |
| France | 1.02 | 2.58 | 1.80 | 0.40 |
| Denmark | 1.22 | 2.78 | 2.00 | 0.40 |
| United Kingdom | 2.12 | 4.48 | 3.30 | 0.60 |
| Italy | 2.22 | 4.58 | 3.40 | 0.60 |
| Germany | 2.92 | 5.28 | 4.10 | 0.60 |
| Israel | 4.03 | 6.77 | 5.40 | 0.70 |
| Canada | 5.23 | 8.37 | 6.80 | 0.80 |
| United States | 6.64 | 10.16 | 8.40 | 0.90 |

In addition to filling out the questionnaire used to construct Table 2, key informants were also interviewed and data from the interviews were coded to analyze the experts' evaluations of the nine relevant factors. Tables 3 and 4 were constructed using data from the interviews. The similarities in the answers across Tables 2, 3, and 4 provide some suggestive support for the reliability of the data. Tables 3 and 4 show the relative frequency of each of the nine factors for entrepreneurial decisions according to the key informants'

**Table 2. Correlation Between Start-up Rate and Factors Relevant for Entrepreneurial Decisions**

| *Cross-country Index* | *Correlation with Entrepr. Propensity* | *Chronbach Alpha* |
|---|---|---|
| Government Policies Helpfulness Index | 0.35 | 0.42 |
| Government Program Helpfulness Index | -0.10 | 0.67 |
| Importance of Financial Support Index | 0.76* | 0.60 |
| Importance of Education and Training Index | 0.67 | 0.77 |
| Ease of R&D Transfer Index | 0.71* | 0.54 |
| Importance of Commercial Infrastructure Index | 0.60 | 0.69 |
| Importance of Internal Market Openness Index | -0.05 | 0.87 |
| Importance of Physical Infrastructure Index | 0.50 | 0.71 |
| Favorable Cultural and Social Norms Index | 0.83* | 0.68 |

*Statistical significance 0.01

interviews. The relative importance shown in Tables 3 and Table 4 does not necessarily imply a negative evaluation of the influence of each specific issue on entrepreneurial propensity but simply indicates that, according to the key informants, those issues are somewhat important. Table 3 shows the relative frequency with which each of the nine factors was identified as the *main issue* by a key informant. That is, it shows what factor among the nine considered is viewed as having the strongest impact on entrepreneurial propensity. For example, the first cell in Table 3 indicates that 19 percent of the Canadian key informants identified government policies as being the main issue for entrepreneurial decisions in their country at the time of the interview. The first cell of the bottom row of Table 3, instead, indicates that, across the 10 countries in the sample, 10 percent of all key informants identified government policies as being the main issue for entrepreneurial decisions as opposed, for example, to cultural and social norms that, instead, were identified as the main issue by 25 percent of key informants across the 10 countries. Of course, as the last two columns before the total one in Table 3 show, several key informants chose as the main issue a factor not listed among the selected nine, while a few others chose not to identify any main issue.

Similarly to the results shown in Table 2, across all 10 countries, several key informants identified cultural and social norms, the availability of equity funding, and the availability of appropriate education and training, as the main issues for entrepreneurial decisions. Fewer key informants identified R&D as the main issue, while virtually no one identified physical infrastructure, market openness, and commercial and legal infrastructure as the main issue facing entrepreneurship in their country. The results for government policy and programs are similar to those reported in Table 2, though the relative importance attributed to the two factors diverges significantly. The first two columns of Table 3 show, for each country, the percentage of key informants who identified government policy and programs, respectively, as the main issue for entrepreneurship in their country. In general, it appears that key informants believe that an entrepreneur's decision to start a new venture is not affected by government programs. This conclusion is consistent across the 10 countries in the sample with the exception, perhaps, of Denmark. Government policies, on the other hand, are identified as the main issue for entrepreneurial decisions by 10 percent of all key informants. Unlike programs, which are insignificant almost everywhere, government policies are clearly much more important in some countries (e.g., Canada, France, Germany, and Israel) than in others.

Each key informant was also asked to select at least three discussion issues among the nine listed factors. If we take the number of times that government policies and programs were discussed during all interviews as an indicator of their significance, their relative importance increases. Table 4 shows the relative frequency with which the nine entrepreneurial factors were identified by the key informants as *discussion issues.* That is, it shows what entrepreneurial factors among the nine considered are viewed as having a strong impact without being the dominant concern for entrepreneurial decisions. Across the 10 countries, government policy and programs represented 14 and 11 percent, respectively, of all issues discussed. With policy issues representing as much as 18 percent of all issues in Italy and Finland, and programs accounting for as much as 19 percent of discussion topics in Denmark.

A qualitative examination of the specific aspects of government policy and programs discussed during the interviews revealed that key informants believed that governments can indeed influence the likelihood of success of new ventures but only indirectly by creating appropriate underlying conditions. Table 5a lists the aspects of government policy that were identified by key informants as being the

**Table 3. Relative Frequency of Factors Influencing Entrepreneurial Decisions Identified as Main Issues**

| | *Governm. Policy* | *Governm. Programs* | *Financial Support* | *Educ. & Training* | *Research. & Dev.* | *Commer. Infrastruc.* | *Market Openess* | *Physical Infrastruc.* | *Social & Cultural Norms* | *Unlisted Main Issue* | *No Main Issue* | *Total* |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Canada | 0.19 | 0.08 | 0.25 | 0.11 | 0.03 | 0.08 | 0.03 | 0.00 | 0.19 | 0.03 | 0.00 | 1.00 |
| Denmark | 0.00 | 0.11 | 0.11 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.33 | 0.44 | 0.00 | 1.00 |
| Finland | 0.05 | 0.00 | 0.14 | 0.14 | 0.00 | 0.00 | 0.00 | 0.00 | 0.43 | 0.14 | 0.11 | 1.00 |
| France | 0.17 | 0.00 | 0.06 | 0.19 | 0.03 | 0.03 | 0.03 | 0.00 | 0.42 | 0.08 | 0.00 | 1.00 |
| Germany | 0.14 | 0.02 | 0.16 | 0.23 | 0.02 | 0.00 | 0.00 | 0.00 | 0.28 | 0.09 | 0.05 | 1.00 |
| Israel | 0.21 | 0.05 | 0.08 | 0.13 | 0.21 | 0.03 | 0.00 | 0.00 | 0.05 | 0.08 | 0.18 | 1.00 |
| Italy | 0.07 | 0.00 | 0.27 | 0.00 | 0.20 | 0.10 | 0.03 | 0.03 | 0.03 | 0.13 | 0.13 | 1.00 |
| Japan | 0.03 | 0.06 | 0.58 | 0.06 | 0.00 | 0.00 | 0.00 | 0.00 | 0.27 | 0.00 | 0.00 | 1.00 |
| UK | 0.00 | 0.00 | 0.00 | 0.29 | 0.05 | 0.03 | 0.00 | 0.00 | 0.45 | 0.05 | 0.13 | 1.00 |
| US | 0.08 | 0.05 | 0.24 | 0.19 | 0.05 | 0.03 | 0.00 | 0.03 | 0.05 | 0.16 | 0.11 | 1.00 |
| All Countries | 0.10 | 0.03 | 0.19 | 0.15 | 0.06 | 0.03 | 0.01 | 0.01 | 0.25 | 0.09 | 0.08 | 1.00 |

**Table 4. Relative Frequency of Factors Influencing Entrepreneurial Decisions Identified as Discussion Issues**

| | *Governm. Policy* | *Governm. Programs* | *Financial Support* | *Educ. & Training* | *Research & Devel.* | *Commer. Infrastru.* | *Market Openess* | *Physical Infrastruc.* | *Social & Cul. Norms* |
|---|---|---|---|---|---|---|---|---|---|
| Canada | 0.15 | 0.12 | 0.26 | 0.10 | 0.08 | 0.06 | 0.06 | 0.02 | 0.15 |
| Denmark | 0.17 | 0.19 | 0.15 | 0.16 | 0.04 | 0.04 | 0.00 | 0.00 | 0.24 |
| Finland | 0.18 | 0.12 | 0.26 | 0.08 | 0.04 | 0.02 | 0.07 | 0.02 | 0.21 |
| France | 0.13 | 0.13 | 0.15 | 0.19 | 0.06 | 0.10 | 0.06 | 0.06 | 0.13 |
| Germany | 0.11 | 0.12 | 0.18 | 0.14 | 0.12 | 0.09 | 0.04 | 0.06 | 0.14 |
| Israel | 0.08 | 0.06 | 0.32 | 0.17 | 0.06 | 0.02 | 0.07 | 0.05 | 0.16 |
| Italy | 0.18 | 0.06 | 0.23 | 0.12 | 0.18 | 0.13 | 0.01 | 0.03 | 0.06 |
| Japan | 0.12 | 0.02 | 0.30 | 0.17 | 0.08 | 0.04 | 0.04 | 0.03 | 0.19 |
| UK | 0.15 | 0.14 | 0.15 | 0.15 | 0.10 | 0.05 | 0.04 | 0.05 | 0.18 |
| US | 0.14 | 0.08 | 0.16 | 0.09 | 0.13 | 0.12 | 0.06 | 0.05 | 0.17 |
| All Countries | 0.14 | 0.11 | 0.22 | 0.13 | 0.09 | 0.06 | 0.05 | 0.04 | 0.17 |

## Table 5. Influence of Government Policy

| *5a. Most Important Aspects of Government Policy Identified by Key Informants as Main Issues* | *Countries** | |
|---|---|---|
| 1. Need for cross-training and sharing of information between government and growing businesses | CA, IL, IT, JP, US | |
| 2. Tax burden is too heavy and is often skewed against smaller firms | CA, FR, IT, US | |
| 3. Burden of compliance with taxes and regulation is high and hinders new firm formation | FI, GE, IT, US | |
| 4. There exist no incentives for developing partnerships between established and new firms, and foreign investors and new firms | CA, FR, IT | |
| ***5b. Most Important Aspects of Government Policy Identified by Key Informants as Discussion Issues*** | ***RI(1)**** | ***RI(2)***** |
| 1. Tax burden is too heavy and is often skewed against smaller firms | 15% | 2% |
| 2. Burden of compliance with taxes and regulation is high and hinders new firm formation | 15% | 2% |
| 3. Need for cross-training and sharing of information between government and growing businesses. In general, governments are sympathetic to entrepreneurs but operate with a very different mindset | 14% | 2% |
| 4. Employment regulation is rigid and has a negative impact on new firms growth | 8% | 1% |
| 5. Other issues | 48% | 7% |

*Country List: CA=Canada, DK=Denmark, FI=Finland, FR=France, GE=Germany, IL=Israel, IT=Italy, JP=Japan, UK=United Kingdom, US=United States.
** The RI(1) column shows the relative importance across countries of that particular topic among all government policy and programs issues, respectively.
*** The RI(2) column shows the relative importance of that particular topic across countries and all nine selected factors.

## Table 6. Influence of Government Programs

| *6a. Most Important Aspects of Government Programs Identified by Key Informants as Main Issues* | *Countries** | |
|---|---|---|
| 1. Need for coordination, stability, and transparency of government programs | CA, FR, GE, IL, IT, JP, US | |
| 2. Need to train government officials to better understand the needs of entrepreneurs so they can design more meaningful programs and provide more useful services and advice | CA, GE, US | |
| ***6b. Most Important Aspects of Government Programs Identified by Key Informants as Discussion Issues*** | ***RI(1)**** | ***RI(2)***** |
| 1. Too many programs exist. No effectiveness evaluation process exists. As a result, ineffective or redundant programs are perpetuated and scarce resources wasted | 28% | 3% |
| 2. Government officials do not know the needs of entrepreneurs. As a result, they are often unable to design meaningful programs and provide useful services and advice. In addition, vehicles for delivering programs often lack sufficient competence | 12% | 1% |
| 3. Decentralization of program delivery works well but there is not enough of it | 7% | 1% |
| 4. Programs are too often based on political interests. As a result, they tend to be unstable and lacking transparency | 5% | 1% |
| 5. Other issues | 48% | 5% |

* Country List: CA=Canada, DK=Denmark, FI=Finland, FR=France, GE=Germany, IL=Israel, IT=Italy, JP=Japan, UK=United Kingdom, US=United States.
** The RI(1) column shows the relative importance across countries of that particular topic among all government policy and programs issues respectively.
*** The RI(2) column shows the relative importance of that particular topic across countries and all nine selected factors.

*main issue* for entrepreneurship in a given country and the countries where the issue was raised. Surprisingly, the primary policy concerns among key informants with respect to policy is the lack of interaction between government and growing businesses. In addition, taxes and the compliance with various regulations and tax laws were considered main issues in four countries. Specifically, Italian and Canadian informants commented not only on the height of the tax rates but also on their distribution across firms of different sizes. Size-related complaints were also raised with respect to regulation compliance being too labor intensive and costly.[12] Finally, the lack of adequate laws on incorporation, initial private offerings and stock options were blamed in three countries for reducing growth incentives for smaller and newer firms.

In addition to the ones listed in Table 5a, other *main policy issues* were identified but only in one or two countries. In Italy and France, for example, key informants identified the main policy issue for the entrepreneurial sector with the fact that institutions that could assist in fostering entrepreneurship suffered from equal representation in their committees of parties that stand on opposite positions regarding new and growing firms. While, in Israel, several key informants identified the broadening of supportive policies, from high-tech start-ups to all new firms, as a necessary condition for the long-term growth of entrepreneurial activity in the country.

The list of aspects of government policy that were identified by key informants as *discussion issues* for entrepreneurship in a given country mirrors that of *main issues.* Table 5b shows that, at about 15 percent each, the top three policy topics listed as main issues are also the three topics more discussed in general across countries. However, when all discussion issues are considered, the rigidity of employment laws becomes relatively more important. The countries where this issue was raised more often were Canada, Finland, Germany, Italy, and the United States. In particular, the cost of labor was the main complaint in Finland and Italy, the rigidity of hiring and firing decisions was the main complaint in Canada and the United States, and restrictive policies in the hiring of foreign workers was the main complaint in Germany.

In this article, government programs refer to the existence, at all levels of government, of initiatives designed to assist new and growing firms. Table 6a shows that, among *main issues,* the primary concerns regarding governmental programs revolve around information about and implementation of programs. In other words, most key informants agreed that although plenty of programs exist, information about them is lacking. Most entrepreneurs are unaware of existing programs and of how to find out about them. Also, a lot of redundancy exists across programs and it is difficult to know when one qualifies. Finally, being delegated to officials who have no adequate background, the implementation of the programs is often unsatisfactory.[13]

Table 6b shows the list of aspects of government programs identified by key informants as *discussion issues.* As in the case of government policy, this list follows closely that of the *main issues.* At 28 percent, the proliferation of programs is identified, by far, as an important problem and a significant source of inefficiency.[14] Also, many of the key informants felt that a more rigorous evaluation of the effectiveness of government programs would be a useful step in eliminating such redundancy. Without an appropriate evaluation process, programs are funded indefinitely, even as new programs with similar services are initiated. Key informants in Germany, Italy, and the United States commented that not enough decentralization of program delivery exists. In addition key informants in Italy and France commented on the lack of transparency and on the connection between politics and programs that makes the latter unstable especially at the local level. In general, the evidence suggests that potential entrepreneurs who are successful in making contact with such programs are more likely to implement a new business, and that those new businesses that make contact for assistance have a higher survival rate and tend to report more growth.[15]

To summarize, government policy and programs seem to be only weakly connected to individuals' entrepreneurial propensity. According to detailed interviews with key informants, they represent only 10 and 3 percent, respectively, of the issues identified as most important (main issues) for entrepreneurship by the 338 key informants. Government policy and programs, however, received more attention as secondary (discussion) issues, where they represent 14 and 11 percent, respectively, of all issues discussed. Among different aspects of government policy, key informants identified the burden of taxation and the high cost of compliance with regulation to be two very important factors. With respect to government programs, instead, key informants indicated redundancy and lack of transparency as being very important. Finally, with respect to both government policy and programs, key informants identified the lack of interaction between governments and growing businesses as a major concern for entrepreneurial activity. That is, differences in information and mindsets between entrepreneurs and public employees were identified as being the main problem hindering the useful deployment of public resources in the entrepreneurial sector. No expert, in any country, suggested or advised the creation of new programs or increased public involvement. Thus, the tendency seems to be that of seeing governments as creators and guarantors of underlying conditions conducive to an entrepreneurial environment rather than as active promoters of entrepreneurial activities.

## Discussion

Entrepreneurs are concerned with the exploitation of profit opportunities. Such opportunities exist in the form of market niches, new ways of producing existing goods, or the introduction of new goods. According to economic literature, entrepreneurship is possible because information is asymmetrically distributed across individuals (Knight 1921) and the entrepreneur is an individual exhibiting above-average alertness (Kirzner 1973, 1979). Thus, by definition, entrepreneurs are individuals who deviate from the mean. They possess a competitive advantage with respect to new methods or products and are, in a sense, ahead of the curve. As a result, the actions of governments with respect to entrepreneurial intervention appear particularly difficult since the number and types of variables that enter the entrepreneurial environment are always changing. These observations are consistent with the results presented in Table 5 and, in particular, Table 6.

A more radical critique on the feasibility of effective government intervention on entrepreneurship would state that it is impossible for governments to gather all the necessary data to begin with, because the necessary information exists in know-how of potential entrepreneurs and is not available to others. In fact, if information were known, superior alertness would not be necessary to exploit profit opportunities. Profit opportunities would be known to everyone and would be immediately eliminated. This is why government intervention and entrepreneurial policy and programs are so difficult to identify. As mentioned by the key informants, entrepreneurs and public officials have different mindsets. The entrepreneurial process underlying entrepreneurial behavior is complex in nature and unpredictable. To a large extent, government policy and programs are variables exogenous to the entrepreneurial process and, given what entrepreneurs do, governments suffer by definition of an informational and mindset disadvantage.

Recent findings on national systems of innovation are consistent with the argument that government intervention with respect to entrepreneurship is extremely hard to plan. A national system of innovation is defined as the web of institutions and economic structures affecting the rate and direction of innovative activities in the economy (Edquist and Lundvall 1993). Much of the research on this subject has shown the bulk of the innovative effort to be endogenous to the economy and sustained by the firms themselves (Nelson 1993). If this argument is accepted, then, with respect to the entrepreneurial sector, governments should promote self-organized and endogenous innovation rather then engage in extensive planning or even selective nurturing. Along these lines, Clark (1988) adopted an evolutionary perspective to discuss forms of public policy that may be appropriate for and conducive to more innovation. Clark's evolutionary argument relied on the observation that the market system is complex and constantly changing and that governments lack information beyond that possessed by entrepreneurs and that, as a result, government policies may not deliver a net positive effect.

Yet, governments do play a crucial role in enhancing the ability of individuals to act entrepreneurially. Although suggestive, results presented in this article support and complement arguments according to which governments need to implement policies that increase market openness and legal transparency (e.g., see Boettke 1993; Brenner 1987; Harper 1996; and Holcombe 1998, 2003). In fact, even if such features of the economic system are important for all businesses, regardless of newness and size, they are particularly important for smaller and newer firms that have lower lobbying power and may not be capable of creating monopolistic rents. Results also suggest that government policy and programs are more effective when capable of enhancing the underlying pool of resources from which potential entrepreneurs draw their inputs than when providing selective safety nets. In fact, the rules and practices that favor innovation and the creation of new markets cannot be imposed by external agencies, but are created, refined, and transmitted effectively over time only if the appropriate institutions and values are transferred across generations. In general, government interventions may be distinguished between proactive government actions specific to entrepreneurship and incentive boosting interventions not necessarily specific to entrepreneurship. Proactive interventions aim at helping those engaged in starting a business and at removing obstacles for their endeavors. Implicitly, proactive interventions assume that perceived or actual barriers discourage prospective entrepreneurs, and that more people would start a business if the process were made easier. Thus, the aim of proactive government intervention is to ease the start-up process and minimize the risk of failure. Incentive type interventions, on the other hand, operate on the principle that entrepreneurs are deterred from entrepreneurship because the expected rewards are not commensurate with the risks, both financial and social.

Although purely suggestive, the results presented in this article indicate that government policy and programs have limited influence on entrepreneurial decisions. Specifically, policy and programs represent only 10 and 3 percent, respectively, of the issues identified as most important (main issues) for entrepreneurship by the 338 key informants. They received, however, more attention as secondary (discussion) issues, where they represented 14 and 11 percent, respectively, of all issues discussed. Among different aspects of government policy, key informants identified the burden of taxation and the high cost of compliance with regulation to be two very important factors. With respect to government programs, instead, key informants indicated redundancy and lack of transparency as being very important. With respect to both government policy and programs, key informants identified the lack of interaction between governments and growing businesses; that is, differences in information and mindsets, as being the main problem hindering the useful deployment of public resources in the entrepreneurial sector. No expert, in any country, suggested or advised new programs or increased public involvement. Thus, the tendency seems to be that of seeing governments as creators and guarantors of underlying conditions conducive to an entrepreneurial environment rather than as active promoters of entrepreneurial activities.

Also, it should be noted that the data refers specifically to 1999. The fact that the data are from a specific year and that if interviewed again the experts might express different opinions is not relevant from a substantive point of view. This is a discussion aimed at generating a debate on structural issues of the economy at the global level. The point of the article is neither country specific nor to evaluate any particular policy or to propose best practices. Rather, the article attempts an evaluation of the ability of governments to influence (positively or negatively) entrepreneurial behavior in general. Within this context, the article does not pretend to offer specific policy prescriptions for any of the countries in the study but, rather, provides further evidence that market processes, as opposed to social constructionism, are more conducive to entrepreneurial behavior. This is consistent with recent studies showing that, when it comes to entrepreneurship, one size does not fit all (Acs et al. 2005) and that much more work is needed at the local and regional level. A very desirable extension of this article, for example, would include longitudinal country-specific studies focusing on the effectiveness (or lack thereof) of specific policy interventions or programs.

The descriptive evidence presented here, however, does support the neoclassical economic view according to which entrepreneurship may be better served by an environment where nascent entrepreneurs may hope in high rewards than by one offering a stronger safety net, and government policy toward entrepreneurship should place greater emphasis on underlying incentive measures rather than specific proactive measures. After all, by definition, entrepreneurship is concerned with the creation of new ventures for the purpose of profit, where the occasion for profit is generated by the entrepreneur's ability to innovate. In several countries, for example, a widespread entrepreneurial sector, capable of adjusting to changes in market conditions, had been one of the main strengths during the stagnation of the early 1990s. When significant changes in relative prices, technologies, and industrial relations exist, entrepreneurial firms demonstrate a remarkable capacity to adjust and innovate and are, therefore, particularly important in smoothing out the effects of the business cycle. It is hoped that governments at all levels will work to provide an environment in which the entrepreneurial spirit may flourish.

## Acknowledgments

The author thanks two anonymous referees for helpful comments and suggestions. Although data used in this work were collected in 1999 by the GEM consortium, their analysis and interpretation as well as any errors are the sole responsibility of the author.

## Endnotes

1. For example, in 1998 the OECD published the report *Fostering Entrepreneurship: A Thematic Review*. This report aims at understanding the state of entrepreneurship in all OECD countries and at identifying which policies might be most successful in fostering it. In 1998, the European Commission presented the report *Fostering Entrepreneurship: Priorities for the Future* to the Council of Ministers. The aim of this report was to simplify the start-up process and improve access to financing throughout the European Union. In addition, many programs including technological incubators, industrial parks, and networks of services have been established in France, Israel, Italy, the United Kingdom, and many other countries.
2. Details about the GEM project and dataset are available at www.gemconsortium.org.
3. Cross-country comparability is, of course, a complex and multilayered phenomenon. How and if countries may be considered comparable depends on the question asked. In this article, comparability refers to aggregate socioeconomic conditions. Thus, examples of relevant indicators include per capita GDP; literacy; mortality rate; life expectancy; educational attainments; legal, commercial, and physical infrastructures; technological levels; and market openness. Data from official international sources, such as the World Bank and the International Monetary Fund, show that the 10 countries in the sample have identical or comparable values for all standard indicators of development. Among others, relevant statistics may be easily obtained from Euromonitor (2005), OECD (2000), and World Bank (2004).
4. Survey respondents were distributed as follows: Canada 1,003; Denmark 1,002; Finland 1,001; France 1,000; Germany 1,008; Israel 992; Italy 1,000; Japan 1,384; United Kingdom 1,014; United States 1,018.

5. The collection of data in the GEM project has undergone significant changes and refinements over the years. The definitions and classifications presented in this article refer exclusively to the methods used in 1999 and should not be used to appraise later data and developments in the GEM project.
6. Reynolds et al. (2005) contains details on the methodology used for the construction and harmonization of the dataset.
7. Details about the selection process used to identify key informants in each country, as well as a list of questions posed to each interviewed individual and other details about the interview process and the data coding can be found in the 1999 GEM *Operation Manual.* The manual is available at www.gemconsortium.com under the heading "1999 documents."
8. An example may clarify the procedure: An academic known for her work on entrepreneurial education could be selected to be a key informant with special knowledge regarding construct #4 *(education and training)*. She would be asked to identify what factor, in her opinion, was the most relevant for the future of entrepreneurship in her country. The selected factor, called the main issue, could be education and training or any of the remaining eight constructs. She would then be asked to identify at least three *discussion issues* (i.e., three factors she considered to be particularly relevant, though not dominant, for the future of entrepreneurship in her country). She would then select, say, *financial support, culture and social norms,* and *internal market openness.* Thus, for each key informant, it was possible to identify the factor each of them believed to be the *main issues* for entrepreneurship plus three additional factors each thought important for entrepreneurship.
9. The complete 1999 GEM questionnaire administered to key informants can be found in the 1999 GEM *Operation Manual,* available at www.gemconsortium.com under the heading "1999 documents."
10. The complete 1999 GEM Report can be downloaded from www.gemconsortium.org.
11. Noticeably, some of the reported Chronbach Alpha's coefficients are low. This is likely due to the fact that they were calculated from the subjective answers of a small number of respondents.
12. In the United States in 1992, for example, it was estimated that regulatory compliance cost small firms approximately $5,000 per employee, versus $500 to $3,400 for larger firms (Zacharakis et al. 1999, p.28).
13. In the United Kingdom, for example, several key informants expressed significant dissatisfaction with the quality of services provided by the system of local agencies specializing in the support of smaller and newer firms.
14. For example, in the United States, in 1999, the state of Wisconsin alone had at least 400 programs providing more than 700 different services for small business, but the overall awareness of their assistance and their use was very low.
15. In Denmark, for example, some key informants identified government programs as a *main issue* and as having a huge positive effect on entrepreneurship in the last decade.

## References

Acs, Z. J., P. Arenius, M. Hay, and M. Minniti. 2005. *2004 global entrepreneurship monitor.* London Business School and Babson College. London, UK, and Babson Park, MA.

Acs, Z. J., B. Carlsson, and C. Karlsson. 1999. *Entrepreneurship, small and medium-sized enterprises and the macroeconomy.* Cambridge University Press, Cambridge, UK.

Amit, R., L. Glosten, and E. Muller. 1993. Challenges to theory development in entrepreneurship research. *Journal of Management Studies* 30: 815–834.

Audretsch, D., and J. A. Elston. 2002. Does firm size matter? Evidence on the impact of liquidity constraints on firm investment behavior in Germany. *International Journal of Industrial Organization* 20, 1:1–17.

Baumol, W. J. 2002. *The free-market innovation machine: Analyzing the growth miracle of capitalism.* Princeton, NJ: Princeton University Press.

Baumol, W. J. 1990 Entrepreneurship: Productive, unproductive, and destructive. *Journal of Political Economy* 98: 893–921.

Birch, D. L. 1987. *Job creation in America.* London: Free Press.

Blanchflower, D. G. 2004. Self-employment: More may not be better. *NBER Working Paper No. 10286.*

Blanchflower, D. G., and A. J. Oswald. 1998. What makes an entrepreneur? *Journal of Labor Economics* 16: 26–60.

Boettke, P. 1993. *Why Perestroika failed: The politics and economics of socialist transformation* Routledge, New York.

Boettke, P., and C. J. Coyne. 2003. Entrepreneurship and development: Cause or consequence? *Advances in Austrian Economics* 6: 67–87.

Bogenhold, D., and U. Staber. 1991. The decline and rise of self-employment. *Employment and Society* 5: 223–239.

Brenner, R. 1987. National policy and entrepreneurship: The statesman's dilemma. *Journal of Business Venturing* 2: 95–101.

Carree, M. A., and A. R. Thurik. 2003. The impact of entrepreneurship on economic growth. In D. B. Audretsch and Z. J. Acs, eds., *Handbook of Entrepreneurship.* Kluwer Academic Publishers.

Carroll, G. R., J. Delacroix, and J. Goodstein. 1988. The political environment of organizations: An ecological view. In: B. M. Shaw and L. L. Cummings, eds., *Research in Organizational Behavior 10.* Greenwich, CT: JAI Press, pp. 359–392.

Clark, N. 1988. Some new approaches to evolutionary economics. *Journal of Economic Issues* 12: 511–531.

Degroof, J. J., E. B. Roberts. 2004. Overcoming weak entrepreneurial infrastructures for academic spin-off ventures. *Journal of Technology Transfers* 29, 3–4:327–352.

Dobbin, F., and T. J. Dowd. 1997. How policy shapes competition: Early railroad fundings in Massachusetts. *Administrative Science Quarterly* 42: 501–529.

Edquist, C., and B.A. Lundvall. 1993. Comparing the Danish and Swedish systems of innovation. In R. Nelson, ed., *National Innovation Systems: A Comparative Analysis.* Oxford: Oxford University Press, pp.265–298.

European Commission. 1998. *Fostering Entrepreneurship: Priorities for the Future.* Report to the Council of Ministers. Brussels.

Evans D., and B. Jovanovic. 1989. An estimated model of entrepreneurial choice under liquidity constraints. *Journal of Political Economy* 97: 808–827.

Evans, D., and L. Leighton. 1989. Some empirical aspects of entrepreneurship. *American Economic Review* 9: 519–535.

Euromonitor. 2005. Global Market Information Database. http://www.euromonitor.com/GMID.

Frederking, L. C. 2004. A cross-national study of culture, organization and entrepreneurship in three neighborhoods. *Entrepreneurship and Regional Development* 16, 3:197–215.

Gartner, W. 1990. What are we talking about when we talk about entrepreneurship? *Journal of Business Venturing* 5: 15–28.

Gartner, W. 1985. A conceptual framework for describing the phenomenon of new venture creation. *Academy of Management Review* 10: 696–706.

Hamilton, B. H. 2000. Does entrepreneurship pay? An empirical analysis of the returns to self-employment. *Journal of Political Economy* 108: 604–631.

Harper, D. 1998. Institutional conditions for entrepreneurship. *Advances in Austrian Economics* 5: 241–275.

Harper, D. 1996. *Entrepreneurship and the market process.* New York: Routledge.

Hayton, J. C., G. Geroge, and S. A. Zahra. 2002. National culture and entrepreneurship: A review of behavioral research. *Entrepreneurship Theory and Practice* 26, 4: 33–52.

Holcombe, R. 2003. The origins of entrepreneurial opportunities. *The Review of Austrian Economics* 16: 25–43.

Holcombe, R. 1998. Entrepreneurship and economic growth. *Quarterly Review of Austrian Economics* 1: 45–62.

Iyigun, M., and A. Owen. 1998. Risk, entrepreneurship and human capital accumulation. *American Economic Review* 88: 454–457.

Jacks, S. L., and A. R. Anderson. 2002. The effects of embeddedness on the entrepreneurial process. *Journal of Business Venturing* 17: 467–487.

Kihlstrom, R., and J. Laffont. 1979. A general equilibrium entrepreneurial theory of firm formation based on risk aversion. *Journal of Political Economy* 87: 719–740.

Kirzner, I.M. 1979. *Perception, opportunity, and profit: Studies in the theory of entrepreneurship.* University of Chicago Press.

Kirzner, I. M. 1973. *Competition and entrepreneurship.* University of Chicago Press.

Knight, F. 1921. *Risk, uncertainty and profit*. University of Chicago Press.

Maggioni, V., M. Sorrentino, and Williams, M. 1999. Mixed consequences of government aid for new venture creation: Evidence from Italy. *Journal of Management and Governance* 3: 287–305.

Markman, G. D., P. Phn, D. B. Balkin, and P. T. Gianiodis. 2005. Entrepreneurship and university-based technology transfer. *Journal of Business Venturing* 20, 2:241–263.

Murphy, K. M., A. Shleifer, and R. Vishny. 1991. The allocation of talent: Implications for growth. *Quarterly Journal of Economics* 106: 503–530.

Nelson, R. R. 1993. *National innovation systems: A comparative analysis*. Oxford: Oxford University Press.

OECD. 2000. OECD Economic Surveys: France (2). http://www.sourceoecd.org.

OECD. 1998. Fostering Entrepreneurship: A Thematic Review. Paris, France.

OECD. 1996. SMES: Employment, innovation, and growth: The Washington workshop. Paris, France: OECD Documents.

Otani, K. 1996. A human capital approach to entrepreneurial capacity. *Economica* 63: 273–289.

Peters, L., M. Rice, and M. Sundararajan. 2004. The role of incubators in the entrepreneurial process. *Journal of Technology Transfer* 29, 1: 83–91.

Porter, M. 1990. The competitive advantage of nations. *Harvard Business Review* 68, 2:73–94.

Reynolds, Paul, Niels S. Bosma, and Erkko Autio. 2005. Global entrepreneurship monitor: Data collection design and implementation 1998–2003. *Small Business Economics* 24, 3: 205–231.

Reynolds, P., M. Hay, and M. Camp. 1999. *Global entrepreneurship monitor: Executive report.* Kansas City, KS: Kauffman Center for Entrepreneurial Leadership.

Spencer, J. W., T. P. Murtha, and S. E. Lenway. 2005. How governments matter to new industry creation. *Academy of Management Review* 30, 2: 321–337.

Stinchcombe, A. L. 1965. Social structure and organizations. In J. G. March, ed., *Handbook of Organizations.* Chicago: Rand McNally, pp. 142–193.

Van de ven, A. H. 1993. The development of an infrastructure for entrepreneurship. *Journal of Business Venturing* 8, 3: 211–230.

Venkataraman, S. 2004. Regional transformation through technological entrepreneurship. *Journal of Business Venturing* 19, 1: 153–167.

Wennekers, A. R., and A. R. Thurik. 1999. Linking entrepreneurship and economic growth. *Small Business Economics* 13: 27–55.

World Bank Group. 2004. World Development Indicators Online. http://devdata.worldbank.org/dataonline.

Wren, C., and D. J. Storey. 2002. Evaluating the effects of soft business support upon small firm performance. *Oxford Economic Papers* 54, 2:334–365.

Zacharakis, A., W. Bygrave, and P. Reynolds. 1999. *GEM—National entrepreneurship assessment: United States executive report.* Kansas City, KS: Kauffman Center for Entrepreneurial Leadership.

## About the Author

**Maria Minniti** (minniti@babson.edu) is an associate professor of economics and an associate professor of entrepreneurship at Babson College. She holds a Ph.D. in economics from New York University and has published numerous articles on entrepreneurship, economic growth, and complexity theory, as well as book chapters and research monographs. Some of her articles have appeared in the *Journal of Economic Behavior and Organizations, Small Business Economics, Journal of Business Venturing, Comparative Economics Studies,* and *Entrepreneurship Theory and Practice.* Dr. Minniti is the research director of the Global Entrepreneurship Monitor (GEM) project, an associate editor of the *Small Business Economics Journal,* and an advisor for the United Nations Development Program.

*Case Study*

# Parting Is Such Sweet Sorrow: DHR Patio Homes, LLC[1] and Family Firm Management

Herbert Sherman
Daniel J. Rowley

*I quit." Those two little words were dropped like an atomic bomb and seemed to explode across the dinner table at the Davis residence. The meal had not yet been served though everyone was at the table engaged in a lively discussion, which of course included their business, DHR Patio Homes, LLC. Immediately, a hush descended upon the Davis family and their guest, close friend, and business associate, Stephen Hodgetts, as an imaginary mushroom cloud filled the room. No one could move or say a word although numerous glances of varying nature were being exchanged in rapid succession. The somberness of the situation was quickly broken, however, by another barrage of discontent. "I've had it, I quit. Find someone else to act as the contractor for the company." With those words, RJ Davis quickly vacated the dining room and zoomed upstairs into the Davises' spare garage apartment.*

## Company History and Background—Part A

### *D&H Management, LLC—A Real Estate Management Firm*

It all started back in August 2002 when the Dow Jones Industrial Average dipped under 8000. Richard Davis and Stephen Hodgetts, academics, friends, and coauthors, were lamenting their ever-shrinking retirement funds. Neither was getting any richer on a faculty member's salary nor expected any windfalls from relatives, their book sales, or lottery tickets. As Hodgetts was fond of saying, "America believes in education: The average professor earns more money in a year than a professional athlete earns in a whole week."[2]

After a long discussion, they decided to become masters of their own economic fate and jump into an entrepreneurial venture. Davis had done enough preliminary research on the real estate market in their area to convince Hodgetts that becoming a landlord was a good idea.

Davis and Hodgetts, with the assistance of the Davis's real estate agent, found six families in three months and worked with these families to find them homes[3] in the $175,000 price range that the families would be happy to lease from Davis and Hodgetts and eventually purchase. The deal was so attractive that they even had a waiting list for new tenants. The six homes, though, had gobbled up their initial investment of $100,000 and required an additional $80,000 (which Hodgetts loaned the company) while their monthly cash flow yielded a net profit of $ 1,500/month. Adrienne, Davis's wife, managed the day-to-day operations of the firm.

### DHR Construction, LLC—A Home Residential Construction Company

The construction company started off as just another small entrepreneurial undertaking to raise venture capital. Hodgetts and Davis would finish off the basements of their rental homes, get the homes reappraised, and then remortgage the properties pulling out an additional $10,000–$20,000 per home. These funds could then be used as down payments for future rental homes.

Davis and Hodgetts were approached by one of their renters to perform all of the nonlicensed work (i.e., framing out the basement, wall boarding, taping, plastering, trimming, painting) to finish off all of the other basements of their tenants. Davis explained to the renters (Alan and Wilma) that they would have to form their own LLC and act as any other subcontractor. Based on the additional funds raised by finishing off the basements, Davis and Hodgetts went on to purchase six more homes, five of which had their basements completed by Alan and Wilma (as A&W Construction, LLC).

Alan and Wilma enjoyed working on these basements since it yielded them additional income of $2,000/month. They approached Davis and Hodgetts about figuring out a way that they could keep occupied year round, however, there was nothing that Davis and Hodgetts could do for Alan and Wilma at that time. Yet a few days later, the situation changed dramatically.

One of Davis's students who was designing their basements said Davis and Hodgetts could cut out the middleman in terms of their rental business if they built their own homes. Davis thought his student was crazy at the time but they talked after class and the student said that he would be happy to act as the general contractor and that he knew all of the subcontractors who were needed to construct new homes. Alan and Wilma would do all of the interior work, and Alan could hire part-time workers to help. In any event, Davis and Hodgetts could build the rest of the homes they wanted to rent under a different company name, sell it to themselves for a profit, and then make a profit renting the homes. On a $150,000 home Davis and Hodgetts would net about a 20 percent profit, that's around $30,000 over a two- to three-month time period (the time it took to build a 1200 square foot three bedroom, two bath home).

The profit derived from this entrepreneurial venture led Davis and Hodgetts to backward integrate their operation; they were now going to build homes not only to be purchased by D&H Management as possible rental units but also for public consumption. In May 2003, DHR Construction broke ground on their first construction site in the St. Andrews development.

In November 2003 Davis and Hodgetts bought out the student's interest in DHR Construction due to differences in management and business philosophy. By January 2004 they had completed three homes at St. Andrews. They then shifted their building site to another location, Florence Development, which they felt had a more upscale look and would allow them to build nicer and more expensive homes. By April 2004 they had built three homes in Florence, had plans to build five more in that area, and were looking at other developments for future growth and expansion. On April 12, 2004, the Florence Development Corporation developed cash flow problems and decided not to pay their landscapers. Each of the properties that were owned by Davis and Hodgetts in the development had a mechanic's lien placed on it by the landscapers for $450,000 per property.

### *DHR Patio Homes, LLC—A Second Home Construction Company*

While a deal was being brokered to clear Davis and Hodgetts' liens, Davis, acting in his usual entrepreneurial manner, located a brand new development in June 2004, about 10 miles east of where they currently were building. The new development, called Snowy Mountains, was a unique project since the developers had built lakes, a golf course, and clubhouse (including a three-star restaurant) and had very specific designs for community development. The housing currently in the development (phase one) ran the gamut of homes, from two-bedroom condominiums (that started around $140,000) to multi-million-dollar estate homes on the lake. Every member of the community was given access to the clubhouse (which included a pool and a playground) and the several lakes dotting the development, as well as given a discount at the restaurant and golf course. The developers also sponsored fishing, golfing, boating, and concert events and even had an island that could be rented for weddings and other parties. The island had fully equipped restrooms with showers, electricity, and a kitchen service cabana.

DHR Patio Homes, LLC was established in August 2004 by Davis and Hodgetts to legally separate their construction projects in Florence (run under the corporate name of DHR Construction, LLC) from their latest project, Mountain Trails, a section of the Snowy Mountain development. Davis and Hodgetts kept the "DHR" designation in the firm's name since they thought that the DHR name had some brand recognition and wanted to show a linkage of ownership between their two construction firms. DHR developed a simple business model. Homes would be priced at 20 percent above cost with Davis acting as the architect and head of construction operations. His job was to work with the subcontractors to ensure that their work met schedule and building code requirements and to make sure that subcontractors' bills coincided with the work provided. Alan would work with Davis as the acting foreman on the job by helping to coordinate the subcontractors as well as continue his own subcontracting work dealing with wall hanging, lining, spackling,

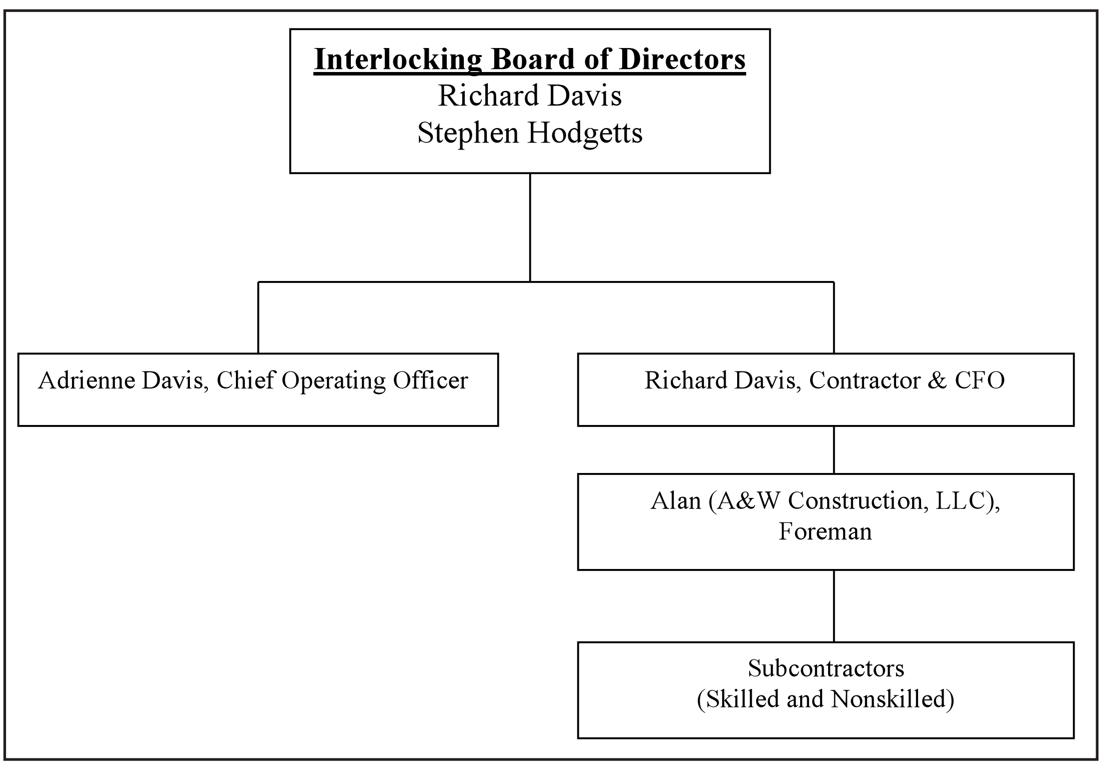



**Figure 1. D&H Management, DHR Construction, DHR Patio Homes (June 2004)**

molding, and painting. Wilma worked along side Alan (though Wilma was paid by Davis and Hodgetts directly) while Alan also hired his younger brother Marvin to help out as there was plenty of work to do and Alan wanted people he could trust. Alan's LLC received $6,000 a month in which to pay himself and his brother and pay federal income tax.

Everything seemed to be going smoothly. Alan was working out quite well, taking over as the foreman and after a while Davis gave Alan carte blanche as to how to run the operational aspects of the construction business (see Figure 1).

## The Latest Debacle

In early January 2005, Davis and Hodgetts changed from using a part-time book bookkeeper to an accountant who worked with numerous home construction businesses. A two-year audit conducted by the accountant on all three businesses revealed that about $25,000 of expenses connected to Alan's corporate credit card account were either for nonbusiness items (i.e., Christmas trees), multiple questionable charges (i.e., filling up the company truck six times in one day), and, at times, was signed by someone other than Alan (signatures on receipts did not match Alan's signature).

After a discussion with their lawyer, Hodgetts and the Davises agreed to confront Alan with their accountants' findings. Evidence was presented as to the inappropriate credit card charges, multiple purchases of gas and tools, and felonious signature on certain credit card charges. Further evidence was presented to Alan that matched his wife's signature to those on the credit card receipts. Alan neither agreed to nor denied the charges. That being the case, Richard took the keys to the company truck and tool shed from Alan and then described to Alan what their continued working relationship would be. Rather than being fired, Alan would be working under his brother (who would form his own company) and his brother's company's monthly check would be docked approximately $4,000 a month until all of the losses had been recovered. Alan still made no comments and left the meeting.

## When In Doubt, Hire Family

Alan's demotion and separation from the business left a wide managerial gap. So who was going to take over as foreman for the month it would probably take to hire a new one? Richard Davis's plans to retire that year and work the business full time had been stymied by the poor cash flow of the business; there was just not enough positive cash flow to pay Davis a salary that was not even half of what he was earning at the university. Davis would continue to act as the firm's CEO but could not devote the time necessary to act as the chief operating officer (foreman). Hodgetts had pursued several academic undertakings (books, articles, and research) in the last year or two with the understanding that he was going to have to be the lead author of this "dynamic duo." He had neither the knowledge of the operational aspects of the construction business necessary to serve in a managerial capacity nor the time needed to supervise home building. None of the owners could then serve as foreman.

Davis and Hodgetts agreed that they would need to recruit a foreman but needed someone immediately (i.e., tomorrow) to fill the position while their search moved ahead. There were two likely candidates who immediately came to mind, both family members. Adrienne Davis, Richard Davis's wife, had an MBA and was managing many of the back office functions for Davis and Hodgetts' three firms. She was quite good at dealing with renters, potential buyers, and suppliers, and served as the information hub for the three firms. RJ, Richard and Adrienne's only child, had already graduated from college and served as an administrative assistant to both a local lawyer and the president of their local hospital. RJ was currently working as the assistant to the president of a personal services firm that happened to be one of Davis and Hodgetts' suppliers and was also providing advertising services through a separate business.

The family, including Hodgetts, had a get-together to discuss this matter and decided that RJ would be the most likely candidate to fill the bill. RJ had the free time, had worked in a very tough and stressful environment (a legal office and a hospital) and excelled, and seemed to have both the interest and tenacity to learn the contracting portion of the business. From Davis and Hodgetts' perspective, this would provide an opportunity to determine whether RJ would want to be the one to eventually take over the family business.

Richard Davis then spent a few days at the work site with RJ to introduce RJ to the numerous subcontractors (plumbers, HVAC, electricians, framers, insulators, carpenters, masons, etc.) and their employees and to spread the word that RJ was going to take over the job of foreman while the business was searching for an experienced person. RJ was pleased to discover that many of the subcontractors had worked together on previous jobs for Davis and Hodgetts as well as for other small local contractors and therefore had developed good working relationships with one another.

No specific managerial training was provided since neither Richard Davis nor Hodgetts had undergone their own managerial training prior to any of their entrepreneurial ventures. Richard did give RJ a copy of all of the building blueprints, work charts (showing which subcontractor had to be working at what time point in each home and what work the subcontractor would perform), and had RJ surf the net to read up on the basics of subcontracting. RJ was a very quick learner and after having several question-and-answer sessions with both Richard and Adrienne, they decided that RJ was ready to go solo on the job site.

## Like March, Coming in Like a Lion

The next day RJ was at the construction site checking in with all of the subcontractors (who were all in the midst of doing their jobs) to make sure that everyone knew what needed to be done by whom and in what order. RJ specifically reminded the electrician that an electrical inspection was to be done in two days on the house he currently was working on and he assured RJ that the he'd be done on time. The electrician was having real problems tracking down some problems he and his coworker were having, both in the basement (the light switches turned on the wrong lights) and in the first floor dining room (electrical outlets were not working and he could not trace the trouble). RJ asked if the inspection should be cancelled or put off for another few days and the electrician again assured RJ that he'd be done on time. (Richard Davis had told RJ that inspectors seemed to get quite mad if they inspected a house that did not seem to be ready. More importantly, the second inspection would be far more thorough and inevitably the inspector would find something on which to fail the electrical inspection.) RJ then called the town hall to ensure that the inspection was properly scheduled and to see what the inspector would need (i.e., blueprints) for his visit.

RJ came home from the first day of the job exhausted and a bit disgruntled. At the dinner table with Richard and Adrienne, RJ described how the electrical problems still had not been solved and how the electrician guaranteed that he'd get the job done even if he had to work through the night to do it. Other problems kept cropping up (i.e., there was a scratch in one of the kitchen cabinets that was delivered and the lighting company shorted them one fixture) and RJ had to be "the problem solver." Many of these problems would throw the building schedule off and RJ was having to constantly shuffle around the subcontractors to accommodate the numerous mishaps found in each home. Richard and Adrienne were empathetic and offered some kindly advice. Richard kept emphasizing how RJ needed to keep the subcontractors up-to-date on the work schedule, while Adrienne asked about the work climate and how the subs were adjusting to their new boss. RJ complained that the temporary nature of the job and RJ's lack of practical construction work experience probably made it more difficult to deal with the subcontractors. How could they respect someone who had never worked in construction before? Like every other challenge, however, RJ would rise to the task.

Richard, in the interim, had found, through a friend of the family, a retired gentleman who had worked in the construction industry for many years. He really only wanted to work part-time, three to four days per week, and felt that he could serve as a foreman if someone else would pitch in to assist on his days off. Richard was really looking for a full-time foreman but kept this gentleman in the back on his mind, just in case.

## A Failed Inspection and Tempers Flare

After a day or two on the job, RJ felt like the work was getting out of control. The lighting fixture supplier still had not delivered one fixture and the electrician seemed absolutely baffled as to what the problem was with the wiring in the dining room, yet did not inform RJ of this until the inspector was at the work site. The inspector subsequently failed the electrical work on the house and left in a huff.

In the interim, problems were starting to arise with a second home since the insulation subcontractor accidentally insulated the house before it could be inspected for framing; the inspector was absolutely livid when he examined the home and refused to inspect it unless all of the insulation was removed. Meanwhile, he noted that there were problems with the framing of the ceiling (warped wood) and that the metal supports for the joists were poorly installed.

RJ's reaction to all of this was very simple. After "playing nice" with the subcontractors who were giving RJ problems, RJ decided to turn hard-hitting and give the subcontractors a tough talking to. The electrician took the brunt of RJ's anger since he did not call RJ in time to cancel the electrical inspection—two houses failing in two days was not a track record that RJ could deal with. The electrician, though apologetic, did not take lightly to RJ's heavy-handed remarks, and returned RJ's comments with some harsh words of his own.

That afternoon RJ confided to Hodgetts, "I feel overwhelmed on the job. How can I handle all of these responsibilities on top of the work I still had to complete for my own small business of writing promotional advertisements?" Hodgetts listened intently to RJ's comments and suggested that RJ either cut back on one of the jobs or speak with Richard and Adrienne about the situation.

## The Calm Before the Storm

The night of the failed electrical inspection, Hodgetts was invited over to the Davis home for dinner so they could discuss the business and see how RJ's first few days on the job were working out. Hodgetts had not revealed his conversation with RJ to the Davises, but the Davises were astute enough parents to know that something was wrong at the work site since RJ seemed more agitated than usual. The dinner conversation started out in its usual jovial manner and then slowly shifted to the progress being made on the construction site.

RJ gave a summary of the past few days, including the failed inspections and the tough time RJ was having managing the contractors. RJ pointed out who all the "good" and "bad" contractors were, and therefore who ended up on RJ's like and dislike list. The Davises and Hodgetts were absolutely silent through RJ's description of the situation (a very difficult task, indeed, for both Richard Davis and Hodgetts) and everyone tried to keep their body language as controlled as possible. RJ finally came to an abrupt finish. This left a long pause for everyone else at the dinner table to fill with table talk or comments about the business. Before anyone could ask RJ a question about the building projects, RJ quit the job and left the room.

## Part B

Adrienne left the table and followed RJ to the spare garage apartment to find out exactly what the problem was. In the interim, Richard Davis and Hodgetts were sitting stunned at the dinner table. The silence was broken when Richard said, "So I guess I'm left holding the bag again! How I'm going to manage to act as contractor again is beyond me, but I've done it before for a short time when we dumped David Russ and I can do it again."[4]

"Slow down," Hodgetts requested, "let's move into the family room and then discuss this matter in a more conducive setting."

While Davis and Hodgetts each resumed their conversation, Adrienne joined them to discuss the matter further. "RJ needs some time to herself," Adrienne began, "and she really is not in a mood to talk right now. Let's give her time to compose herself and perhaps she'll come down to chat with us."

"That's fine by me," quipped Hodgetts, "I lost my appetite on the first 'I quit.' Adrienne, perhaps you can tell us what this is all about?"

"What this is about," started Richard, "is the fact that I'm going to have to clean up this mess and get back into the day-to-day operations of the business. I'm going to need to get to the bottom of the problems with the subcontractors and clear up this chaos."

"Yes, yes, yes," jumped in Hodgetts. "That's all well and good, Richard, but we have to get at the root of the matter with RJ—what could have made her quit in only a few days? She has been in jobs with far more pressure than this and yet here she collapses like an accordion on the first sign of trouble? What's going on here?"

"She wouldn't tell me," Adrienne declared, "and I certainly was not going to pressure her. That's all she would need right now, an overbearing mother!" With that last sentence Adrienne's gaze quickly affixed on her husband, Richard, who clearly got the hands-off message.

## The "Truth" Wills Out

About a half an hour later, RJ came down and joined the threesome to discuss the work situation. Rather than pepper RJ with a series of questions, the group allowed her the opportunity to let her story unfold.

> I knew that I was a young woman walking into a man's world, even for a short time, and I thought I was prepared for what I would encounter—discrimination and sexual harassment. I treated everyone fairly but tough and wanted to come across as the boss, especially with those subcontractors who were not getting the job done. I wanted them to be afraid of me, that I would fire them on the spot if the work didn't get done well and on time, that I was a person to be reckoned with; a bitch. The subs saw me replace our former foreman Alan and knew that if he could be replaced, they all could. I thought that is what I needed to do to earn the respect of the subcontractors—in a tough world, be tough.
>
> Though they were polite enough when talking with me directly, I overheard several subs talking with their coworkers about me, and, trust me, it was not complimentary. What really got me upset was that they kept referring to me as "that woman" and that I was less than competent because of my gender.
>
> Worse, the presence of a woman on the job site seemed to be a distraction to some of the subs' employees, especially the younger, unmarried workers.[5] One of them kept asking me out on a date, which, of course, I continued to say "no" to; and I explained that it was a conflict of interest for us to become socially involved. I further asked him to stop asking me out and that I felt uncomfortable with his advances. This clearly did not deter his advances, which I kept putting off. When I eventually threatened to have him fired if he didn't back off, he finally got my point.
>
> It was immediately clear to me that it did not matter what I said; the subs were going to do their thing and deal with Dad if there were any real problems; like failing an inspection is not a problem! I felt out of place and in the way. I quit because it was apparent that in that environment there was no way, no how, that I could work with the subs and get the work completed in a productive, timely manner.

Richard Davis's face said it all. Anger for how his daughter was treated, regret that he had put her into an untenable situation, and guilt on his part for thinking that she had dumped this problem on him for no real reason. Adrienne also wondered how she might have prepared RJ for this situation though Adrienne had never experienced anything close to what RJ had described.

While Adrienne comforted her daughter, both Richard Davis and Hodgetts discussed the matter further, knowing that they would still have to deal with these issues as well as the need to find an immediate replacement for RJ.

*Editors' Note:* Anyone wishing to obtain the instructor's manual for the case study should contact Dr. Herbert Sherman at Herbert.Sherman@liu.edu.

## Endnotes

1. This is a disguised case. The names of the firms and characters have been changed by request of the owners.
2. http://www.quotationspage.com/search.php3, August 27, 2003.
3. The location has been purposely left out to support the disguised nature of the case.
4. For an earlier case study on DHR Construction, see Sherman, Herbert, and Daniel James Rowley. 2004. Case study: DHR Construction, LLC: Parts A and B. New England Journal of Entrepreneurship 6, 2: 33–44.
5. These workers were a mixture of immigrants and locals and included men of Hispanic origin.

## About the Authors

**HERBERT SHERMAN** (Herbert.Sherman@liu.edu) is a professor of management at the Brooklyn campus of Long Island University (New York). He received his Ph.D. in strategic management from the Union Institute and University in Cincinnati, Ohio. Dr. Sherman teaches undergraduate and graduate courses in management and marketing strategy. His research interests include business strategy, case writing and research, business ethics, and education administration. He has published his work in several journals, including the *Journal of Business Ethics, Entrepreneurship and Regional Development, Case Research Journal, Management Decisions,* and *Planning for Higher Education.* Dr. Sherman recently coauthored a book entitled *Strategic Management: An Organizational Change Approach* (University Press, 2006) and is completing a coauthored textbook in business, government, and society. He is the newly appointed editor of the *New England Journal of Entrepreneurship* and the former editor of the *Journal of Behavioral and Applied Management and The CASE Journal.*

**DANIEL JAMES ROWLEY** (daniel.rowley@unco.edu) is a distinguished professor of management of the Monfort College of Business at the University of Northern Colorado, teaching courses in business strategy and international management. He is the lead author of four scholarly books on strategic planning in colleges and universities; a workbook in the same series; a book on academic supervision; and a textbook on business strategic management with Dr. Sherman. He is the author of articles, cases, and presentations on these subjects nationally and internationally and has forthcoming articles in *Emerald's* 2007 *Handbook of Business Strategy* and *Strategic Planning for Public Research Universities.* He has served as editor and as associate editor of the *Journal of Behavioral and Applied Management,* and has published book reviews and article reviews in several different journals including *Learning and Education.* He received his B.A. from the University of Colorado at Boulder in 1969; his MPA from the University of Denver in 1978; and his Ph.D. from the University of Colorado at Boulder in 1987.

# Capital Accessibility, Gender, and Ethnicity: The Case of Minority Women-owned Firms

Leyland M. Lucas

*Minority women continue to make significant gains in economic activity, particularly as entrepreneurs through the creation of small businesses. Despite this increased role in small business activity and an admirable rate of success, minority women-owned businesses continue to experience problems in acquiring capital. This difficulty, which some have attributed to discriminatory practices, forces a large number of these businesses to rely on governmental support programs for assistance in meeting their capital needs. Building on the idea that things are not as simple as commonly presented, a case is made that access to capital for women-owned businesses is affected by a number of other factors tied to the inability to join important networks.*

Small businesses are an essential tenet of the U.S. economy and continue to be created in increasing numbers. According to recent census estimates, small businesses account for more than 35 percent of economic activity and will continue to increase despite changes in the qualifying criteria. Within this broad sector of the economy, even more rapid growth is occurring in the creation and successful operation of small businesses owned and operated by minority women. The number of these firms has been increasing at a faster rate than that of minority males (U.S. Census Bureau 2002), suggesting that minority women-owned businesses are taking on an increasingly important role in the U.S. economy.

Despite continued growth in minority women-owned businesses, attempts by government, private banking, and boutique lenders appear unable to fulfill the need for capital generated by these businesses. As a consequence, many minority women-owned businesses are unable to secure capital for reasons such as unacceptable rates of return, concentration in low-profit industries, and incompatible risk exposure (Greene et al. 2001; Mason and Harrison 1999; Timmons and Bygrave 1997). As a result, stories persist of the challenges that minority women-owned businesses face in accessing capital. Further complicating the issue is the fact that set-aside programs and stereotypical attitudes that view these owners as "too soft" and incapable of making the tough decisions persist are seen as hampering the development of these businesses.

Although these stories persist, there are other valid reasons why minority women-owned businesses have difficulty in accessing capital. The intent of this article is to suggest that, while these attitudes persist, there is a more rational explanation why minority women-owned businesses find access to capital so difficult. We suggest that lending decisions are driven by issues of profitability, return on investment, and the perception that investments are "relatively safe." Such determinations can be made by examining the experience of entrepreneurs, information accessibility, liabilities of newness and size, and management styles. These factors rather than the persistence of prejudice and stereotypical attitudes explain why many minority women-owned businesses find access to capital so difficult.

The next section reviews some of the critical aspects of women and minority-owned businesses. It is followed by arguments and the development of propositions that explain the challenges to capital accessibility among minority women-owned businesses. The article concludes with a discussion of possible implications for these businesses and policy-makers in assessing strategies to increase capital accessibility.

## Critical Aspects of Minority Women-owned Businesses

The essence of entrepreneurial activity is opportunity recognition, timing, and exploitation. Entrepreneurship cannot flourish unless all three of these factors converge. Failure in any one of these areas leads to unfulfilled entrepreneurial goals and objectives. It is the convergence of these three factors that has led to the substantive increase in small business activity.

Having access to capital markets requires knowledge about who has capital available and for what purposes. In reality, however, this knowledge is not perfectly available and minority women entrepreneurs often find themselves at a disadvantage in this respect, because they are not part of the important networks that play a role in the capital markets. To further complicate the issue, minority women entrepreneurs, in their quest for capital, are entering a male-dominated setting and lack the necessary social contacts and skills (Cliff 1998; Greene et al. 2001; Uzzi 1999). The dominance of males in this setting leads to the adoption of specific values and beliefs that appear at odds with those of women. As a consequence, lending to minority women entrepreneurs is seen as a high-risk venture that is unlikely to provide adequate returns.

## Conceptual Development

Success in business often depends more on who knows you and what they know about your work than on either what or whom you know. If these entrepreneurs are known to individuals who are part of important networks, then it is easier for information about these entrepreneurs to be shared than in instances where they are not part of these informal networks. Additionally, informal networks often provide significant and valuable information that can either enhance or counter what is already known about an entrepreneur's character.

## *Experience*

Small businesses are often established by individuals who recognize an opportunity closely related to their current employment. This is particularly the case where these businesses are designed to offer services previously performed by the company but now targeted for outsourcing. To best exploit these opportunities, entrepreneurs must not only recognize that they exist but also have experience that is viewed as critical to the success of their operations (Fiet et al. 2002; Haynes and Haynes 1999; Lerner and Almor 2002). The substance of the argument is that capital exists and lenders are willing to accommodate the needs of entrepreneurs so long as they have the relevant experience and are not pursuing "pies in the skies" dreams (Humphreys and McClung 1981; Schwartz 1976).

Two types of experience are critical to business success and, by extension, access to capital: general and specific (Sigrist 1999). General experience, or business experience, is acquired through the opportunity to work in a large or small corporate body and participate in the making of significant decisions (Humphreys and McClung 1981; Schwartz 1976). Such general experience may be acquired through one's corporate career that may involve opportunities at a single or several corporate entities. Specific experience, or industry experience, is much narrower in scope and deeper in quality because it typically covers exposure to significant decision making within the same industry. Specific experience is idiosyncratic to the particular circumstances surrounding an industry. Through specific experience, an individual gains greater insight into the intricacies of the business cycle as it pertains to a particular industry (Brophy 1989; Coleman 2000; Loscocco and Robinson 1991). These different types of experience are addressed more fully below.

## *Business Experience*

A critical aspect of business experience is that it provides individuals with access to human capital, which is the stored knowledge and abilities possessed by individuals (Birley et al. 1987). This is achieved through access to occupational experiences that allow individuals to develop skills on several aspects of business that prove to be essential for the creation and operation of successful businesses. Without this human capital, individuals are likely to make critical errors in decisions and these can prove fatal for the business. Anecdotal evidence suggests that this is already a problem among small businesses and contributes to their high failure rates.

Recent studies have found that women now occupy more than 15 percent of senior corporate positions and the number of female chief executives has tripled within the past seven years (Downey 2002). However, these gains among women are not matched by gains among minority women. Though their numbers in undergraduate and graduate fields of study are increasing, minority women in business are highly concentrated in support roles and fields that afford little opportunity for significant senior management experience. The concentration of minority women in these support roles provides them with limited access to the requisite business experience helpful to establishing successful businesses. Although their undergraduate training provided insight into financing, accounting, marketing, and other skills necessary to perform critical business functions, some of the more intricate skills that can only be acquired through exposure to critical decision-making in a "real-world" scenario are not acquired. Minority-women entrepreneurs tend to be well educated. However, they often lack training in critical areas of business that can provide access to important networks (Brush 1992; Lituchy et al. 2004).

The limited business experience has major implications for minority women entrepreneurs to access capital. These difficulties arise because minority women are not part of the critical networks that can provide them with the information needed to gain the business experience (Fabowale 1995; Loscocco and Robinson 1991). For several reasons, minority women find that they are more often involved in tightly knit networks that have few linkages to major players outside of the network. It is access to the players who are outside of the network that are positioned to provide these women with the opportunities to acquire significant business experience and access to capital. In effect, the strong ties established by minority women prevent them from establishing weak ties that create access to funding opportunities. Strong ties provide minority women entrepreneurs with, at best, very narrow business experiences that are often confined to a few areas. Weak ties provide minority women entrepreneurs with broad business experiences that significantly increase their breadth of learning and widen their access to major players who can expose them to multiple funding options (Humphreys and McClung 1981; Schwartz 1976).

Therefore, we suggest that business experience has major consequences for the minority women entrepreneur's efforts to access capital. Because most minorities are concentrated in support roles in businesses, their skill base is limited. A limited skills base means that the human capital developed by these entrepreneurs lacks many of the important skills and exposure necessary to operate successful businesses. If these entrepreneurs do not have the requisite knowledge important in making sound business decisions, then lenders are unlikely to provide capital. Lenders want to ensure that individuals entrusted with the task of investing assets have the skills to make good business decisions. Furthermore, concentration in support roles results in minorities developing strong ties that further limit their exposure to critical individuals who might help to develop their skills base. By maintaining strong ties, minorities are unable to create multiple weak ties with individuals who can provide them with access to other skills and who can provide access to capital. From these arguments we draw the following proposition:

**Proposition 1:**
**Minority women entrepreneurs lacking significant business experience will find it increasingly difficult to access capital.**

## *Industry Experience*

Even when minority women entrepreneurs have significant business experience, the relevance of that experience to their entrepreneurial ventures may create additional problems. Minority women entrepreneurs may be required to have specific industry experience. Significant industry experience suggests that entrepreneurs understand what is important in the industry, know who are the key players, and can better assess trends and opportunities for entrepreneurial activities (Brophy 1989; Coleman 2000; Loscocco and Robinson 1991). Studies have shown that previous experience plays a critical role in the success of small businesses, especially when that experience is within the same industry where these small businesses operate (Brush and Hisrich 1988; Srinivasan, Woo, and Cooper 1994)

Research in this area shows that women owners with access to human capital, particularly in the form of significant senior management experience, and higher levels of education are more likely to access capital than their counterparts without these qualities (Haynes and Haynes 1999; Lerner and Almor 2002). Minority women entrepreneurs with knowledge of the industries in which they operate know what is important to the industry, its trends, and key players. These women, who successfully rose to senior management positions, can use the knowledge and information they acquired to make crucial decisions on which the relative success/failure of their businesses might depend. Their industry experience helps them to better craft their ideas and to provide a well-developed plan of action. With a well-developed plan of action, they can determine what sources of capital can be pursued, which prior relationships can facilitate access to capital, and how prior relationships with capital sources can secure better financing terms.

Moreover, minority women entrepreneurs with industry experience not only know the industry but also know some of the "key players." This knowledge helps to reduce information obstacles that limit other entrepreneurs from accessing certain sources of capital. This gives them some legitimacy in the industry among potential financiers who may have dealt with them in the past. If these women have established a good reputation among these potential financiers through their previous contacts, then they will find it much easier to access financing. For instance, access to venture capital is more a function of whom one knows than it is of the viability of the business idea (Brush 1992). From these arguments, we develop the following proposition:

**Proposition 2:**
**Minority women entrepreneurs with significant prior industry experience will likely find it easier to access capital than those without significant industry experience.**

## *Information Accessibility*

Successful entrepreneurs must have access to financial resources. Access to these resources requires that some trusting relationship be developed between the entrepreneur (agent) and the lender (principal). This trusting relationship is particularly important from the perspective of the principal who must be sure that the agent will (1) adhere to the conditions under which the funding has been provided, and (2) has the ability to repay the loan. Trust is essential between the principal and agent because of information asymmetries due to liabilities of newness and smallness (Lant and Mezias 1992). Small businesses, particularly those that are private, do not provide a high quality and quantity of information from which informed decisions by lenders can be made (Berger and Udell 1995; Ennew and Binks 1997). Information essential to the loan decision-making process is unavailable, and faced with this paucity of information, lenders make decisions to deny funding.

In addition to the issues raised previously, an important factor that affects access to capital is information. Prior research has suggested that capital inaccessibility is a result of high search costs both for lenders and entrepreneurs (Wetzel 1987). The gist of the argument is that capital exists, but lenders are frustrated in their efforts to provide capital because entrepreneurs are not hooked into the networks that provide information on capital availability. This lack of information persists despite efforts by governmental and other agencies to provide entrepreneurs with information on capital availability. Consequently, failure to find capital has a discouraging effect whereby entrepreneurs, given the scarcity of resources and the high costs of search, cease to pursue potential lending opportunities (Mason and Harrison 2002).

Although absence of information may affect access to capital, of even greater importance is the type of information that can facilitate a successful search. Information acquired must not only provide the entrepreneur with the idea of where capital exists, but also what type of capital exists. In essence, information acquired to facilitate the "meeting" between entrepreneur and capital source must be both general and specific, as they both affect the credit decision-making process (Jensen and Meckling 1992). General information refers to what is widely known not only about the business, but also about the environmental conditions affecting this business (Uzzi and Lancaster 2003). Specific information is idiosyncratic to the particular circumstances surrounding a business.

Although both general and specific information are important to the loan decision-making process, lenders must often deal with incomplete information. Incomplete information results because women-owned businesses, like other small businesses, are often privately held and not subject to the reporting requirements of publicly held institutions (Brush 1992; Hisrich, 1989).

Incomplete information increases ambiguity and the risks associated with a borrower. Prospective lenders find it more difficult to (1) assess the borrower's ability to comply with loan agreements, (2) determine whether the borrower has certain relevant capabilities, and (3) meets lender's requirements (Ennew and Binks 1993). Incomplete information limits the ability of lenders to make an "informed" assessment of the potential borrower.

Lenders can counter these risks in one of three ways. One option is to increase the collateral requirement for borrowers. Increase in collateral requirements, particularly when it involves personal assets, is seen as an intrinsic motivator to success. The borrower knows that failure to meet expectations will result in a loss of the collateral, which may include very prized personal assets. Several studies have found that pledging collateral often facilitates borrowing among small businesses (Ang et al. 1995; Broome 1990). A second option is to increase the rate of interest. Charging higher rates of interest not only reflects risk levels, but also helps to compensate for information asymmetry and exposure of lenders to greater risk (Petersen and Rajan 1994). A third option available to lenders is to pursue lending relationships primarily with long-term customers. With long-term relationships, lenders have the opportunity to observe performance, financial and otherwise, and develop additional information that would not necessarily be available. Long-term relationships provide additional information, improve the quality of the relationship between the lender and borrower, and increase the likelihood that the borrower will adhere to the conditions stipulated in the loan agreement.

However, there are problems with all three of these options. With respect to pledging increased collateral, financial institutions are in the business of lending money and not in the business of managing and liquidating assets. Performing these functions places additional burdens on lenders that can be eliminated through more selective lending. Although lenders can also compensate for risk by charging higher interest rates, there is a point beyond which managing such loans is not feasible. Beyond a specific threshold, the benefits from maintaining high rate/high risk loans are far outweighed by their costs. Building long-term relationships is not an option for many women-owned businesses because most are relatively new. In addition, recent decisions within the banking industry to centralize the loan decision-making process reduce the value of building long-term relationships, especially when many of those relationships would have been built with branch personnel no longer involved in the loan decision-making process (Uzzi and Lancaster 2003). The challenges associated with each of these options not only increase the risk potential of lending to these businesses, but also the cost of lending for both parties. Minority women businessowners are forced to borrow at higher interest rates and lenders incur additional monitoring costs. From these arguments, one can draw the following proposition:

**Proposition 3:**
**Information accessibility will have a significant influence on access to capital for minority women entrepreneurs.**

## *Liability of Newness*

The age of a business affects its performance, and its ability to survive. New businesses lack the broad bases of influence, endorsement, and stable relationships with important constituents. New businesses suffer from a liability of newness and this translates into a greater likelihood of failure (Baum and Oliver 1991; Carroll 1983; Stinchcombe 1965). Newer businesses are more vulnerable to environmental shocks because they are still in the process of developing an understanding of how the industry works (Lant and Mezias 1992). In addition, these new businesses have not yet established the important linkages that may affect their awareness of environmental forces, industry trends, and emerging opportunities. Older small businesses have survived the liability of newness, while younger ones are yet to show that they have survived this liability (Lant and Mezias 1992). By surviving the liability of newness, women-owned small businesses have demonstrated that they have the ability to be competitive, rather than remain stagnant and die.

Older minority women-owned small businesses that have survived the liability of newness may be better positioned to access capital. With older businesses, more information is available about their performance. By surviving, these businesses have demonstrated the ability to "do things right." Moreover, as these businesses age, management is better able to delegate responsibility and concentrate on strategic issues. Roles are more clearly defined and higher levels of trust exist. As small businesses grow older more information about them becomes available. Although there is a tendency to keep information private, some information does seep into the public domain permitting lenders to make more informed decisions regarding loan applications than would be the case for new small businesses. From these arguments, one can draw the following proposition:

**Proposition 4:**
**Older minority women-owned small businesses will find it easier to access capital than their younger counterparts.**

## *Liability of Smallness*

The decision to either grow or remain small is a strategic one that every entrepreneur must consider. Opportunities to grow may exist, but decisions against growth may be made because the businessowners are risk-averse and this may continue even as wealth increases (Brown and Segal 1989; Jianakoplos and Bernasek 1998; Olsen and Currie 1992). By maintaining a relatively small operation, minority women maintain their risk-aversion and limit their need for capital. Small firms require less need for external capital particularly if they do not operate in capital-intensive industries. By maintaining relatively small businesses, minority women entrepreneurs can rely on their personal savings and retained earnings for funding of expansion. Decisions regarding growth have implications for resource endowment, capital requirements, and capital structure (Greene and Brown 1997). It also raises issues regarding control, a subject that may be critical to minority women entrepreneurs. As minority women entrepreneurs increase their debt-equity ratio, the degree of control over their operations decreases. The actions they undertake are increasingly subject to the oversight of external parties more concerned with ensuring loan repayment than in the long-term survival of the business. By opting to remain small, these businesses are constrained in achieving their full potential. Constraints on growth may subsequently harm these minority women-owned businesses because their client base is less diversified than would otherwise be the case. This lack of diversification further exposes these small businesses to fluctuations of the business cycle.

The emphasis on maintaining small businesses translates into what had been termed "the liability of smallness." Small businesses have a greater likelihood of either dying or failing to access much needed capital because they can be effectively screened out of the population without significantly affecting the level of competition. This is referred to as "the impact of niche width" (Freeman et al. 1983; Levins 1968; Loscocco and Robinson 1991). Niche width is defined as a population's tolerance for factors that inhibit growth. The greater the tolerance for growth inhibitors, the broader is the perceived niche width.

One important characteristic of niche width is spatial distribution, which is the extent of variety. When patterns are difficult to identify, spatial distribution is said to be high, otherwise it is low. The existence of significant numbers of small businesses in the service sector suggests that there are large groups of homogeneous businesses and a lack of spatial distribution. The existence of large groups of homogeneous small businesses increases the possibility for low profit margins and allows lenders to be more selective. The more marginally profitable small businesses have a higher propensity for failure because they operate close to the margin and find it more difficult to attract resources, including capital. As a result, lenders are more selective in their loan decisions. Given the abundance of small businesses, lenders can then pay less attention to the marginally profitable businesses and focus on lending to the more profitable ones.

Thus, issues of control and spatial distribution may result in minority women entrepreneurs operating small businesses that lenders may be less willing to fund. Several of these businesses operate at or close to the margins and this translates into a greater likelihood of failure. The closer a small business is to the margins, the lower is the capital available to absorb cyclical fluctuations in economic activity. From a lender's perspective, low profit margins also decrease the potential for debt repayment. With an overabundance of small businesses, lenders can be more selective in their loan decision-making choosing to focus on more profitable businesses rather than expose themselves to greater risk of loan default. From these arguments, one can draw the following proposition:

**Proposition 5:**
**A preference for maintaining small businesses by minority women entrepreneurs will limit their ability to access capital.**

## Conclusions

Small businesses continue to act as an important source of economic growth and play a critical role in the U.S. economy. Coupled with this role has been a significant growth in the number of minority women-owned small businesses. To support this growth, several programs have been designed to further promote their chances for success. Despite these efforts, problems still persist for minority women businessowners. One problem many of these businessowners face is accessing capital. Though some have suggested that inaccessibility to capital is a result of discriminatory policies, this article makes the argument that inaccessibility occurs because minority women entrepreneurs are often absent from important networks. These important networks help in skill development, provide entrepreneurs with access to critical information, and help to facilitate the views formed about their abilities to operate small businesses successfully.

While issues of discrimination may prevail, there are other reasons why women entrepreneurs find it difficult to access capital. Lack of access to capital can be explained by inexperience, information inaccessibility, and liabilities of newness and size—all of which are in some way related to the need to become part of the important networks. Capital will be provided to businesses that have demonstrated the ability to be highly profitable and successful. The objective of lending is to secure an adequate return on investment. If businessowners show that their businesses are viable, then funds will be made available. Failure to demonstrate viability of a business is not a function of discrimination but due to certain idiosyncratic conditions operating within small businesses and among small businessowners.

Minority women businessowners must take a different approach to accessing capital rather than the ones currently used. Faced with these idiosyncratic conditions in the small business segment, these businessowners must find ways to counter the perceived gaps in their abilities. For instance, focusing on relationship banking may help in the long run but is of little value in the short term. Therefore, minority women businessowners might consider finding ways to increase information availability.

Finally, although minority women businessowners need to adopt new approaches in accessing capital, generating behavioral change is not easily achieved. It is a process that can only be pursued over time and the results of such change may be difficult to discern. Small businesses operate in changing environments and, as these businessowners enact change, old challenges will disappear and new ones will emerge. Therefore, minority women businessowners must find ways to either anticipate new challenges or counter them. The fact that women businesses continue to grow despite these challenges to capital access may show some hope for the future.

## References


Ang, J. S. et al. 1995. Evidence on the lack of separation between business and personal risks among small businesses. *Journal of Small Business Finance* 4: 197–210.

Baum, J.A., and C. Oliver. 1991. Institutional linkages and organizational mortality. *Administrative Science Quarterly* 36: 187–218.

Berger, A.N., and G. F. Udell. 1995. Relationship lending and lines of credit in small business finance. *Journal of Business* 68: 351–382.

Birley, S., et al. 1987. Do women entrepreneurs require different training? *American Journal of Small Business* 12: 27–35.

Broome, J. 1990. A loan at last? *Nation's Business* 82: 40–44.

Brophy, D. J. 1989. Financing women-owned entrepreneurial firms. In O. Hagan, C. Rivcum, and D. Sexton, eds., *Women-owned businesses.* New York: Praeger.

Brown, S.A., and P. Segal. 1989. Female entrepreneurs in profile. *Canadian Banker* (July–August): 32–34.

Brush, C. 1992. Research on women business owners: Past trends, a new perspective and future directions. *Entrepreneurship Theory and Practice* 16: 5–30.

Brush, C., and R. D. Hisrich. 1988. The women entrepreneur: Strategic origins—impact on growth. *Frontiers of Entrepreneurship Research*. Babson Park, MA: Center for Entrepreneurial Research, Babson College.

Carroll, G. R. 1983. A stochastic model of organizational mortality: Review and reanalysis. *Social Science Research* 12: 303–329.

Cliff, J. 1998. Does one size fit all? Exploring the relationship between attitudes towards growth, gender, and business size. *Journal of Business Venturing* 13: 523–542.

Coleman, S. 2000. Access to capital and terms of credit: A comparison of men- and women-owned small businesses. *Journal of Small Business Management* 38: 37–52.

Ennew, C., and M. Binks. 1993. Financing entrepreneurship in recession: Does the banking relationship constrain performance? In N. C. Churchill et al., eds., *Frontiers of Entrepreneurship Research.* Babson Park, MA: Center for Entrepreneurial Studies Babson College, 481–495.

Ennew, C., and M. Binks. 1997. Information asymmetries, the banking relationship and the implications for growth. In N. C. Churchill et al., eds., Frontiers of Entrepreneurship Research. Babson Park, MA: Center for Entrepreneurial Research, Babson College.

Fabowale, L. et al. 1995. Gender, structural factors, and credit terms between Canadian small businesses and financial institutions. *Entrepreneurship, Theory & Practice* 19: 41–67.

Fiet, J., et al. 2002. Still searching (systematically) for entrepreneurial discoveries. *Small Business Economics* 25: 489–515.

Freeman, J. H., et al. 1983. The liability of newness: Age dependence in organizational death rates. *American Sociological Review* 88: 1116–1145.

Greene, P., and T. Brown. 1997. Resource needs and the dynamic capitalism typology. *Journal of Business Venturing* 12: 161–173.

Greene, P., et al. 2001. Patterns of venture capital funding: Is gender a factor? *Venture Capital* 3: 63–83.

Haynes, G. W., and D. C. Haynes. 1999. The debt structure of small businesses owned by women in 1987 and 1993. *Journal of Small Business Management* 37: 1–18.

Hisrich, R. D. 1989. Women entrepreneurs: Problems and prescriptions for success in the future. In O. Hagan, C. Rivchun, and D. Sexton, eds., *Women business entrepreneurs*. New York: Praeger.

Humphreys, M. A., and H. McClung. 1981. Women entrepreneurs in Oklahoma. *Review of Regional Economics and Business* 6, 2: 13–20.

Jensen, M. C., and W. H. Meckling. 1976. Theory of the firm: Managerial behavior, agency costs and ownership structure. *Journal of Financial Economics* 3: 305–360.

Jensen, M. C., and W. H. Meckling. 1992. Specific and general knowledge and organizational structure. In L. Werin and H. Wijkander, eds., *Contract Economics*. Cambridge, MA: Blackwell Publishers.

Jianakoplos, N. A., and A. Bernasek. 1998. Are women more risk averse? *Economic Inquiry* 36: 620–630.

Lant, T. K., and S. J. Mezias. 1992. An organizational learning model of convergence and reorientation. *Organization Science* 3: 47–71.

Lerner, M., and T. Almor. 2002. Relationship between strategic capabilities and the performance of women-owned small ventures. *Journal of Small Business Management* 40: 109–125.

Levins, R. 1968. *Evolution in changing environments.* Princeton, NJ: Princeton University Press.

Lituchy, T., and M. Reavley. 2004. Women entrepreneurs: A comparison of international small business owners in Poland and the Czech Republic. *Journal of International Entrepreneurship* 2: 61–87.

Loscocco, K. A., and J. Robinson. 1991. Barriers to women's small business success in the United States. *Gender & Society* 5: 511–532.

Mason, C., and R. Harrison. 2002. Barriers to investment in the informal venture capital sector. *Entrepreneurship & Regional Development* 14: 271–287.

Mason, C., and R. Harrison. 1999. Venture capital: rationale, aims, and scope. *Venture Capital* 1: 1–46.

Olsen, S., and H. Currie. 1992. Female entrepreneurs: Personal value systems and business strategies in a male-dominated industry. *Journal of Small Business Management* 30: 49–57.

Petersen, M., and R. Rajan. 1994. The benefits of lending relationships: Evidence from small business data. *Journal of Finance* 49: 3–38.

Schwartz, E. B. 1976. Entrepreneurship: A new female frontier. *Journal of Contemporary Business* 5: 47–76.

Sigrist, B. 1999. *Entrepreneurial opportunity recognition.* Presented at the Annual UIC/AMA symposium at Marketing/Entrepreneurship Interface. Sofia-Antipolis, France.

Srinivasan, R., C. Woo, and A. Cooper. 1994. Performance determinants for male and female entrepreneurs. *Frontiers of Entrepreneurship Research.* Babson Park, MA: Center for Entrepreneurial Research, Babson College.

Stinchcombe, A. L. 1965. Social structure in organizations. In J.G. March, ed., *Handbook of organizations.* Chicago: Rand McNally, 153–193.

Timmons, J. A., and W. D. Bygrave. 1997. Venture capital: Reflections and projections. In D.L. Sexton and R. Smilor, eds., *Entrepreneurship 2000.* Chicago: Upstart Publishing, 29–46.

U.S. Census Bureau. 2002. Survey of women-owned firms. Washington, DC: U.S. Department of Commerce, Economics and Statistics Administration.

Uzzi, B. 1999. Embeddedness in the making of financial capital: How social relations and networks benefit firms seeking financing. *American Sociological Review* 64: 481–505.

Uzzi, B., and R. Lancaster. 2003. Relational embeddedness and learning: The case of bank loan managers and their clients. *Management Science* 49: 383–399.

Wetzel Jr., W. E. 1987. The informal venture capital market: Aspects of scale and market efficiency. *Journal of Business Venturing* 2: 299–314.

## About the Author

**Leyland M. Lucas** (llucas@moac.morgan.edu) is an associate professor of management in the Earl Graves School of Business & Management at Morgan State University. He received his Ph.D. in organization management from Rutgers University. Dr. Lucas has published papers in *Entrepreneurship Theory & Practice, International Journal of Technology Management, Journal of Knowledge Management, The Learning Organization, and Journal of Applied Management & Entrepreneurship.* His research interests include organizational search, knowledge management, opportunity recognition, minority and women-based entrepreneurship, and innercity entrepreneurship.

# The Embedded Entrepreneur: Recognizing the Strength of Ethnic Social Ties

Ed Chung
Kim Whalen

*This article is premised on the idea that social networks represent an important, but often overlooked, unit of analysis in management and entrepreneurship studies. The concept of embeddedness, emphasizing the significance of social relationships, is of particular relevance as more and more frequently minorities and immigrants engage in small businessownership. This article borrows from the ethnicity and social network traditions, and offers that an analysis of the ethnic homogeneity of an entrepreneur's strong and weak social ties would be fruitful in gauging entrepreneurial success.*

## Introduction

In much of the management and marketing literatures, the unit of analysis is often the individual. The entrepreneurship literature has more or less followed this path, and a large body of insightful work has flourished under this agency perspective. McKay and Chung's (2005) discussion of benchmarking for entrepreneurial survival (and success) highlights the emphasis that has been placed on the individual—the entrepreneur—in question. In their study of factors that lead to small business success, Rutherford and Oswald (2000) specifically focused on attributes of the owner/manager, placing the individual squarely at the core of entrepreneurial performance. In a similar vein, Becherer, Halstead, and Haynes (2003) studied the level of marketing orientation in entrepreneurial firms, based primarily on data gathered on key individuals—the CEOs of small firms.

These and other similar studies have enriched our understanding of entrepreneurial effectiveness. Certainly, the entrepreneur plays a vital role in the success of a small business. However, because entrepreneurial pursuits are but a subset of the human condition and because the human condition cannot be fully studied without also examining social forces, the embeddedness perspective offers an opportunity to develop a more complete understanding of entrepreneurial success (Alexander and Smith 1993; Emirbayer and Goodwin 1994; Chung and Fischer 1999a).

In recent years, small businessownership by minority groups and immigrants has grown at a much faster clip than the national average. While in 1997 minority firms made up only 14.6 percent of all U.S. firms, the percentage share of minority firms in total U.S. business is growing. Between 1992 and 1997, the growth rate in number of minority-owned businesses was significantly larger than that of nonminority businesses (The State of Minority Business 2001). In fact, the growth over the past two decades has been significant. In 1982, minority-owned firms represented only 6.8 percent of all U.S. firms, but this figure grew to 9.3 percent in 1987, 12.5 percent in 1992, and as mentioned above, 14.6 percent in 1997 (Minority Business Statistics 2005). In terms of specific minority groups in the United States, Asian-owned businesses grew by 24 percent between 1997 and 2002, black-owned businesses grew in number of firms by 45 percent, and Hispanic-owned businesses grew by 31 percent (Survey of Business Owners 2002). The apparent propensity for minorities and immigrants to enter small businessownership has triggered many studies comparing entrepreneurial startup and success across various cultures (e.g., Tienda and Raijman 2004). Cultural and ethnicity considerations compound the challenges of studying the minority entrepreneur, and here the inadequacy of an individualistic approach is particularly glaring.

In this article, we suggest that entrepreneurship studies should pay special attention to businesses owned and started by minorities and migrants, and that such a focus would benefit greatly from a socially embedded approach. To simplify our discussions, we limit our attention to minority entrepreneurs, though by no means do we suggest that all minorities are immigrants, or that all immigrants are minorities.

## Social Processes and Migration

Cultural values are shaped in part by social and individual processes (Chung 2000). Indeed, interpersonal relationships can even play a role in the emergence of certain ethnic groups. Glazer (1954/c.1964) recounts how a number of ethnic groups came into existence after the people migrated to America. Along this line of an emerging ethnicity, Tilly (1990) also notes that (p.84)

> By and large, the effective units of migration were (and are) neither individuals nor households but sets of people linked by acquaintance, kinship, and work experience. . . . Where kinsmen, friends, neighbors, and work associates already have good contacts. . . [migrants] rely on these networks for assistance both in moving and in settling at the destination.

According to Tilly, these networks often create new categories (ethnic groups), and in so doing, provide the basis for ethnic identity. And if, as previous research seems to suggest, ethnic identity affects consumer behavior, it would then be beneficial to learn more about the social relationships of migrants.

How an immigrant adjusts to his or her new environs is largely determined by the immigrant's social relationships, and whether social networks represent a help or hindrance to the immigrant's acculturation is the subject of ongoing study (Kwong 1984; Pohjola 1991; Portes and Sensenbrenner 1993).

## A Socially Embedded Approach

Many researchers reject the notion that social behavior is caused by attitudes and norms alone. In the study of interpersonal relationships, a strong research tradition has been established in the realms of network analysis (e.g., Brown and Reingen 1987; Granovetter 1982; Ward and Reingen 1990). One implicit assumption of network analysis, called the "anticategorical imperative," stresses the significance of structural and social relationships in shaping social behavior (Emirbayer and Goodwin 1994). The idea that social networking is important to entrepreneurial firms is not new. For example, Peng's (2001) study of Chinese entrepreneurs suggests that networking is one of the major entrepreneurial strategies used by practitioners. The importance of social influences and relationships on behavior has long been recognized by consumer researchers (e.g., Rogers 1976). In this line of thinking, analysts question the usefulness of approaches that stress only the nonrelational attributes and/or purposive actions of individuals. Out of this recognition stems various attempts to incorporate social relations in the study of human behavior.

Central to this social perspective is the idea that people are "embedded" in social relationships. In offering his argument of embeddedness, Granovetter (1985, p.482) notes, ". . . the behavior and institutions to be analyzed are so constrained by ongoing social relations that to construe them as independent is a grievous misunderstanding."

Because most people do not live alone in caves, but instead interact with one another in a society where relationships are formed, the embeddedness perspective proposes that social structure "constrains, supports, or derails individual goal-seeking behaviors" (Portes and Sensenbrenner 1993, p.1321). In simple English, embeddedness means that the company one keeps has an impact on one's behaviors.

Granovetter's (1985) concept of embeddedness contrasts sharply with the "undersocialized concept" of human action, which is characteristic of the economic perspective. According to Granovetter (p.490), the fact that people generally prefer to deal with individuals with known reputations "implies that few are actually content to rely on either generalized morality or institutional arrangements [governance structures] to guard against trouble [deceit]." But even when economists take into account the role of reputation, they do so in an "undersocialized" fashion by generalizing it as a mathematical ratio. Embeddedness, as in a network of interpersonal relationships, is critical in "generating trust, in establishing expectations, and in creating and enforcing norms" (Coleman 1988, p.S97). Moreover, our relationships with others also play a role in developing and maintaining our own identities and self-concepts, particularly in terms of the relative salience of our various discrete identities (Stryker 1968).

The embeddedness argument was presented by Granovetter (1985) in the context that economic action is embedded in social relations. Specifically, he referred to the role of social networks in generating trust and discouraging malfeasance, and the behavior of interest was economic behavior. While economic action took center stage in Granovetter's discussion, economic behavior was only used as an illustration. Indeed, as Granovetter noted (1985, p.504), "most behavior is closely embedded in networks of interpersonal relations and that such an [embeddedness] argument avoids the extremes of under- and oversocialized views of human action. . . . I believe this to be so for all behavior."

## The Importance of Interpersonal Relationships

It is well established in sociology that feelings of identity are distinct from social relationships and exert varying influences on behavior (Oliver 1984; Tilly 1978). Social relationships, for instance, are seen by many social-movement researchers as a key determinant of activism (Gould 1991; McAdam and Paulsen 1993; Rosenthal et al. 1985). In the social movement literature, many studies have shown that psychological and attitudinal factors provide only limited explanation for individual participation (McAdam and Paulsen 1993). For example, in a study of a peace demonstration in the Netherlands, Klandermans and Oegema (1987) have found that 96 percent of those who were attitudinally or psychologically disposed to participate did not do so. This emphasizes that psychological and attitudinal factors are not always enough of a motivation to lead to activism.

Adoption and diffusion researchers have also incorporated social relations in their analysis of how innovations are communicated over time. Indeed, interpersonal influences represent one of two integral components of how information is transmitted and opinions formed (Burt 1987; Gatignon and Robertson 1985; Mahajan, Muller, and Bass 1990; Rogers 1976). Another research area that has benefited from a social relationships perspective is the study of job-seeking behavior, and related to that, the diffusion of information (Granovetter 1982; Liu and Duff 1972; Weimann 1983). Consequently, under the embeddedness approach, a detailed analysis of social structure is central to an understanding of social action, of which "economic action is seen only as a special, if important, category" (Granovetter 1985, p.507).

The importance of social relationships is not lost on consumer researchers either. Belk (1988), for example, suggests a broader sense of self that includes not only the individual level, but also a collective level such as family, group, and cultural levels. He proposes that the concept of an extended self is "a central construct that can explain a variety of consumer and human behaviors" (p.160) more completely than the narrower individual sense of self. Frenzen and Davis (1990), building on the idea of embedded markets, note that market behavior is explained not by economic utilities alone but also by preexisting social relationships between buyers and sellers.

In view of the criticism leveled at the atomization perspective, in which focus is placed on the individual as the unit of analysis, many researchers have incorporated the concept of groups in their work, or even as the focal point of their studies. Childers and Rao (1992), for example, study the influence that reference groups have on the consumption of luxuries and necessities in the United States and Thailand. Ho (2005) employed a dyadic perspective to study social influence on psychological contract fulfillment. Interpersonal influence is recognized as an important set of influences in diffusion research (Mahajan et al. 1990; Midgley and Dowling 1993). Bearden, Netemeyer, and Teel (1989) undertake the task of developing a scale to measure consumer susceptibility to interpersonal influence. Brown and Reingen (1987) perform a network analysis of word-of-mouth referral behavior. Ward and Reingen (1990) study group decision-making and reason that strong social ties lead to greater belief sharing among group members. And as we noted earlier, Frenzen and Davis's (1990) study concerns consumer behavior in embedded markets. These and other important studies have sparked growing interest in the social aspects of human endeavors, by alerting researchers to the contributions that investigations into social relationships may bring. While much of past research was mainly centered on individual action, this stream of analysis acknowledges that humans are social beings and as such are influenced by the company they keep. As Venkatesh (1995) has remarked, ". . . all consumer behaviors (are) primarily sociocultural phenomena that must, therefore, be discussed in sociocultural terms" (p.29). The important point is that we are seeing more research sensitive to the importance of social relationships, which helps to alleviate some of the problems associated with the "undersocialization" criticism.

Embeddedness is not an entirely new concept in the study of firm behavior. Indeed, as Gnyawali and Madhavan (2001) point out, structural embeddedness, or the analysis of interfirm network influences on competitive behavior, has been given some attention in the literature. Our article continues on this path by incorporating entrepreneurship inquiry into this stream of research.

## Social Networks and the Minority Entrepreneur

According to data from the 2000 Census, immigrants have higher self-employment rates than do natives (Toussaint-Comeau 2005). Oftentimes, social networks influence the type of business a minority entrepreneur will open. In fact, businesses owned by minority entrepreneurs are often concentrated in small niches (Masurel, Nijkamp, and Vindigni 2004). For instance, *USA Today* (2002) reported that Koreans own 29 percent of Asian food stores. Vietnamese own 37 percent of Asian nail-care salons. Asian-Indians own more than half of all economy lodging properties in the United States. During the tech boom in Silicon Valley, more than 25 percent were owned by Asian-Indian or Chinese entrepreneurs. Data from the 2000 Census on the most common businesses for entrepreneurs from several different minority groups is consistent with the above minority group and business pairings (Toussaint-Comeau 2005). Clearly, social networks are important for minority entrepreneurs.

Funding issues are particularly challenging for minority entrepreneurs. Many of them, lacking significant personal financial sources, rely primarily on governmental assistance (*Entrepreneur Magazine* 2003). However, as various governmental entities begin to look for ways to reduce spending, increasingly so minority entrepreneurs look to social networks as a way to secure financing, be it through venture capital or social circles. As Erkki Liikanen of the EU remarked in a conference on ethnic entrepreneurship in Brussels in 2003 (Europa 2003), most ethnic minority entrepreneurs rely heavily on coethnic social networks to help them get started with their businesses. These networks, however, are often closed to those who are not part of the social network, and even when available, tend to be limited in their resources or expertise. A study by the Canadian government indicated that 30 percent of visible-minority entrepreneurs cited financing as a key obstacle in starting their small businesses (Industry Canada 2005). Even so, as reported in *USA Today* (2002), the success and proliferation of Asian entrepreneurs in the United States owes much to the availability of what is called "informal loan associations" that are essentially based on coethnic social networks.

The concept of social capital facilitates an understanding of embedded social relations to which Granovetter alluded. Coleman's (1988) discussion of the various forms of social capital provides a starting point for investigating how social relations influence human action. Instead of merely criticizing economists for their undersocialized views and sociologists for their oversocialized conception of human behavior, Coleman proposes a tool that "involves use of the paradigm of rational action but without the assumption of atomistic elements stripped of social relationships" (Coleman 1988, p.S118). Inkpen and Tsang (2005) applied the concept of social capital to the study of knowledge transfer among network members. Indeed, new energy is beginning to infuse the relatively old concept of social capital, as more researchers start to "rediscover" its efficacy (Adler and Kwon 2002).

Portes and Sensenbrenner (1993) modify the idea of social capital for application in a migration context. Their study focuses on minority immigrant groups, and offers an interesting recasting of social capital in a more "ethnic" light. Of particular interest is their idea of "bounded solidarity" as a kind of social capital that minority immigrant groups have to offer, as well as the changing nature of bounded solidarity itself.

According to Portes and Sensenbrenner (1993), bounded solidarity is a collective consciousness that compels people to behave in a certain way. Bounded solidarity does not come from some underlying moral order, but emerges as a collective sentiment, a defensive strategy (of the group) arising out of feelings of oppression, etc., what Portes and Sensenbrenner (1993, p.1325) called a "defensive banding together of the losers in the market struggle." This kind of social capital is situational, and is a group *reaction* made necessary by a common adversary. It is bounded because it is restricted to members of a particular group who are similarly and contemporarily affected by common events. In developing this concept, Portes and Sensenbrenner borrow from Marx's notion of class struggles, referring to migrant ethnic solidary communities as born out of a confrontation with the host society.

Portes and Sensenbrenner note that a group needs to be able to "activate a cultural repertoire" in addition to using group defense to sustain bounded solidarity. Thus, confrontation helps to build bounded solidarity, and activating a cultural repertoire helps to sustain it. But not all immigrant groups develop this sense of solidarity. Some do not have to, and some do not want to. On this latter point, Wang's (1991) concept of sojourner's mentality is illustrative. Those migrants who do not plan to stay, but are contemplating exit, may not see a need for solidarity at all, since they would perceive fewer "clashes" with the host society (Portes and Sensenbrenner 1993). Contrast the solidarity of earlier ethnic Chinese immigrants to Canada with the lack of it among more recent Chinese immigrants (Johnson 1992; Kwong 1984). Sojourner's mentality alone of course does not fully explain why recent immigrants may exhibit less solidarity. As Johnson (1992) has noted, higher education levels (and thus occupational mobility) and a multicultural policy by the Canadian government have contributed to a less problematic adaptation. But many of these recent immigrants consider their stay temporary and look forward to "going home" (Wang 1991). In this respect, they have less need to form solidary communities united by common interest or to belong to them. Instead, as Johnson (1992) has reported, ethnic organizations are no longer defense strategies against the host society's overt prejudice and discrimination, but are voluntary associations that offer other appeals.

While some minority migrants closely identify with their ethnic groups, and socialize frequently in those circles, there are also minority migrants who do not do so. Such intracultural differences have been identified in the consumer culture literature (e.g., Chung 2000) and in studies on ethnic enclaves (e.g., Light et al. 1994). We propose that such intracultural differences exist among minority entrepreneurs. Various factors lead to such differences, and these differences have varying consequences on entrepreneurial behavior.

A lot of work has been done on how "ethnic" one feels. More precisely, much has been done on how closely a person identifies with her or his ethnic group. Much of this takes an individualistic approach, as we have alluded to earlier. From a more sociological perspective, following Chung and Fischer (1999a), we propose that the ethnic homogeneity of a person's social ties, and their relative strength, have a lot to do with how "ethnic" the person is. This borrows heavily from Granovetter's (1985) work on social ties.

## The Strength of the Tie

How do "interactions in small groups aggregate to form large-scale patterns," Granovetter asks (1973, p.1360). The answer, according to Granovetter, lies in the use of weak ties as bridges over which new ideas are transmitted from group to group. Social relationships vary in their tie strength, which Granovetter sees as "a combination of the amount of time, the emotional intensity, the intimacy and the reciprocal services which characterize the tie" (p.1361). Thus, friends would be typified by strong ties, while acquaintances would be characterized by weak ties. "Absent ties" refer to a lack of any relationship or ties that do not have real significance. In Granovetter's scheme of things, regularly buying a morning paper from the same vendor does not lend to a tie. Thus, strong ties are basically close relationships.

While the strength of the weak ties argument is persuasive and has received much attention in the literature, strong ties are by no means moribund in their impact on our lives. Indeed, Granovetter, in a subsequent (1982) revision of his weak ties theory, concedes that strong ties also play a significant role. Other researchers have suggested that strong and weak ties exert differing influences on human action (e.g., Brown and Reingen 1987).

Weak ties may be important bridges over which information is diffused, while strong ties are sources of social influence on our actions. How does this reflect the ethnic*ness* of a person?

## Ethnic Homogeneity of Interpersonal Relationships

While closeness or strength appears to be the common way of thinking about social relationships, it is but one approach to the analysis of social connectivity. Researchers using the "relational analysis" perspective of social structure are not limited to studying only tie strength (Emirbayer and Goodwin 1994). Indeed, it is the patterns of interaction that lays the empirical foundation of network analysis, and the mere existence of ties is itself meaningful and consequential (Cook and Whitmeyer 1992). We propose that in the context of ethnic groups, following the lead of scholars in the field of ethnic enclave economies (Light et al. 1994; Portes 1984), the ethnic homogeneity of one's social relationships is also an important consideration.

## Ethnicity and Strength of Ties

Thus, a useful examination of interpersonal relationships comprises both the ethnicity and strength of one's social ties. Coethnic relationships are those with people of the same ethnic background, while nonethnic relationships refer to those with people from ethnic backgrounds different from one's own. Ethnic homogeneity of strong ties, then, refers to the preponderance of coethnics among a person's close relationships. Likewise, ethnic homogeneity of weak ties refers to the preponderance of coethnics among a person's peripheral relationships.

If, as the literature seems to indicate, a person's strong ties exert important influence over the person's behavior, we would expect that the more ethnic one's strong ties are, the more "ethnic" one's behavior would be.

On the other hand, weak ties, as conduits of information, may well play an important role in a migrant consumer's knowledge of the products and services that the host society has to offer.

Since most migrants look to coethnic ties to help with their adjustment to a new society (Kwong 1984; Pohjola 1991), this could have important social policy implications as well, not the least among which has to do with the questions of ethnic economy and ethnic enclave economy (Light et al. 1994).

## Ethnic Ties and Entrepreneurship

Social ties appear to have varying effects on people, depending on the strength of the ties. The ethnic homogeneity of one's social ties, as we have seen above, influences people's propensity to behave in a more or less "ethnic" manner. In the context of entrepreneurial activities, this may well translate into the kind of social capital one desires or relies on among others of a similar ethnic heritage. It may also influence whether the entrepreneur would target specific ethnic market segments given her or his own ethnic background. It may, furthermore, affect the location of the firm, the makeup of its workforce, the suppliers and facilitating institutions (Dunne and Lusch 2005) one uses, and so on. Facilitating institutions refers to members of the supply chain that facilitate the buying and selling in a supply chain, but who do not take title. These include institutions such as purchasing agents, ad agencies, transportation companies, financial enterprises, and the like.

From the above discussion, we offer the following propositions:

**Proposition 1: The more the ethnic homogeneity of an entrepreneur's strong ties, the more likely the firm's markets and products will be ethnic in scope.**

**Proposition 2: The less the ethnic homogeneity of an entrepreneur's strong ties, the more likely the firm's markets and products will extend beyond ethnic boundaries.**

**Proposition 3: The more the ethnic homogeneity of an entrepreneur's weak ties, the more likely the firm's management processes and facilitating institutions will be ethnic in scope.**

**Proposition 4: The less the ethnic homogeneity of an entrepreneur's weak ties, the more likely the firm's management processes and facilitating institutions will extend beyond ethnic boundaries.**

While there are certainly advantages to be had by engaging in the kind of niche marketing typified by a minority-owned SME operating within the confines of an ethnic environment, opportunities for growth are more abundant if the firm were to expand beyond being an ethnic operation. Moreover, to the extent that access to a wider range of facilitating institutions than what the ethnic enclave could offer is advantageous, one would expect that firms with wider access would achieve better survivability or performance. With this in mind, we offer the following additional propositions:

**Proposition 5: Firms whose products and markets extend beyond ethnic enclaves outperform those that primarily serve ethnic communities with ethnic products.**

**Proposition 6: Firms whose management processes and facilitating institutions extend beyond ethnic communities outperform those who rely on processes and institutions within the ethnic communities.**

## Measuring Strength of Ethnic Ties

To test the above propositions, we need to identify and measure two important sets of variables. First, we need to isolate an entrepreneur's social network and distinguish between the strong ties from the weak ties. Second, we need to measure the ethnic homogeneity of the entrepreneur's strong ties, and likewise for her or his weak ties.

Network analysis is a common method of identifying relationships and an individual's social network. When performing network analysis, first we typically identify all of the connections a person has in a given social context (e.g., membership in an organization), and second we classify these ties by measuring them on certain dimensions such as tie strength (e.g., Sirsi et al. 1996; Ward and Reingen 1990). Another approach that researchers have utilized in studying social relationships is to begin with categories of ties, rather than all the relationships a person has (e.g., Argyle 1986). This approach is generally useful when the ties in question are not constricted by a specific membership or organization. There are at least two related strategies for data collection in this respect.

First, a "rules for social relationships" stream examines what people see as acceptable behaviors (thus "rules") given a particular kind of relationship. In this kind of research, relationships are classified based on their roles. Examples of such roles include spouse, date, teacher, coworker, and so on. For instance, previous research by Argyle and his colleagues (e.g., Argyle, Graham, and White 1979) establish a list of between 22 to 25 kinds of relationships that are found to apply across a range of cultural settings.

A second line of inquiry categorizes relationships based on the significance the individual places on the relationship. Instead of roles, investigators are interested in how much the relationships mean to people. Fischer (1982), in his attempt to discover what people mean by "friend," finds that it is a very common label and to some extent a residual label. McAdam and Paulsen (1993) analyze people's decision to take part in the 1964 Mississippi Freedom Summer Project, to determine the sources of support for actual participation. Having identified social relationships as a key variable, McAdam and Paulsen ask individuals to indicate all those "who positively influenced your decision to apply to the Freedom Summer Project" (p.652). The researchers find that participants were greatly influenced by those with whom they had closer interpersonal ties; the latter were self-identified by the subjects when asked to "list at least 10 persons whom they (applicants) asked to be kept informed of their summer activities" (p.652). Typified by McAdam and Paulsen's approach, these studies (e.g., Chung and Fischer 1999b) begin with certain descriptions of relationship categories and ask respondents to list those individuals who they believe fit each description.

Chung and Fischer (1999b) describe the methodology that they used to both identify strong and weak ties and to measure the ethnic homogeneity of the strong and weak ties. First, participants identify their own ethnic affiliation with a four-item, five-point scale based on Donthu and Cherian's (1992) ethnic identification scale. Second, the participants' social network is identified. Participants are asked to indicate which individuals they would interact with given several different scenarios. The strength of the identified ties is measured via a five-item scale by Sirsi et al. (1996). Lastly, the ethnicity of both the strong and weak ties is determined. Participants are asked to indicate if the ethnicity of the individuals identified as part of their social network matches their own ethnicity. Ethnic homogeneity is quantified as the percentage of the ties that are with individuals with matching ethnicity. Thus, strong and weak ties are identified and the ethnic homogeneity of these ties is measured.

## Modeling Entrepreneurial Success

Recently, McKay and Chung (2005) proposed a model for benchmarking entrepreneurial survival (in the context of their paper, continued survival of an entrepreneur firm is considered a success given the high failure rates). They outlined four "exemplary processes" that they felt should be "central in an entrepreneur's benchmarking." These processes are: cooperation, sharing founder's vision, time management, and developing organizational competency. Unfortunately, McKay and Chung (2005) did not offer concrete suggestions as to how their various models may be measured. While our current study does not lend itself to an elaboration of McKay and Chung's model, and indeed we have simply added to it, we believe it would be fruitful for future research to fully address the measurement issues thus posed.

Particularly in light of Propositions 5 and 6, we propose that for minority-owned SMEs, another important benchmark would be the ethnic homogeneity of the entrepreneur's strong and weak ties. In this respect, we would add to the McKay and Chung model a fifth benchmark, that of ethnic homogeneity of ties (see Figure 1).

## Discussion

Increasing numbers of minorities and immigrants see entrepreneurship as an alternative to traditional occupations in the corporate sector. Not only do researchers need to continue their examination of factors leading to entrepreneurial success, but also they must be cognizant of the additional complications that an ethnic dimension throws into the equation. Furthermore, our article is a departure from the typical unit of analysis, where the individual entrepreneur is the central focus. Indeed, we propose that the phenomenon of entrepreneurship cannot be comprehensively studied without due attention paid to sociological forces, through interpersonal relationships, which play a part on the human condition. In this respect, our study contributes to extant literature by introducing first an ethnic dimension to entrepreneurial research, and second, by highlighting the critical role that social forces play. In their editorial comment in the *Academy of Management Journal,* Ireland, Reutzel, and Webb (2005) urged researchers not only to continue to foster the robust field of entrepreneurial research, but also to

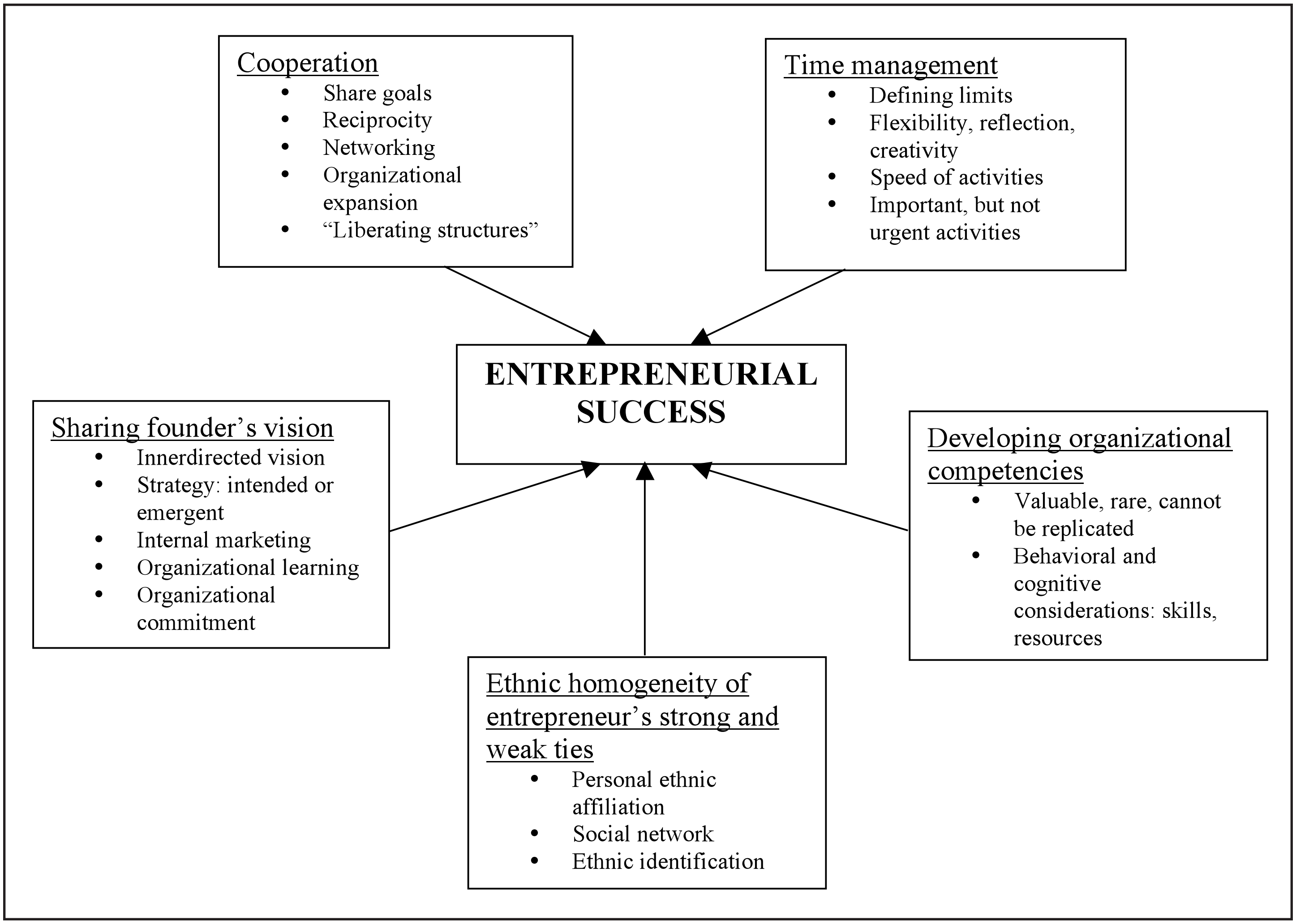



**Figure 1. Modeling Entrepreneurial Success**

consider the question: Where does business (and in our context, entrepreneurs) come from? Our research is consistent with this line of inquiry, and we hope that our introduction of social ties into entrepreneurial research will further what Ireland et al. predict to be a "robustness of talent and diversity of insights" in this area.

We borrowed from the framework proposed by McKay and Chung (2005), in which they suggested that four processes need to be benchmarked to help facilitate entrepreneurial success. To this we added our fifth benchmark, in the context of minority-owned SMEs, that of ethnic homogeneity of strong and weak ties. A series of propositions are offered in our study to test our overall hypothesis that social relationships and ethnic ties matter. In addition, we discussed a solution to the potential data collection problem of researching open-ended social networks.

SMEs are fueling much of the economy and job creation. In particular, minority- and migrant-owned SMEs represent not only an important part of our economic system, but also one of vital significance to minority and migrant communities.

Our article highlights various areas that may fruitfully be addressed by future research. In particular, research is needed in the areas of ethnic social ties among entrepreneurs, for example to arrive at a more parsimonious measure of the strength of ethnic ties. How such social ties may relate to an entrepreneur's sense of ethnic identification may well be a rewarding area of research. In addition, we believe the literature would be enriched by future research into our modified model of entrepreneurial success. While we offer, primarily based on McKay and Chung's (2005) discussion, the key constructs and some of their variables, currently the literature does not contain sufficient guidance to help us develop a full-scale research study around the topics. We suggest that more work needs to be done on developing the measures required before the McKay and Chung (and our modified) model can be tested. Admittedly, while the above places a lot of burden on future research, we recognize the importance of building a strong foundation on which to premise any substantive testing of our propositions.

## References


Adler, Paul S., and Seok-Woo Kwon. 2002. Social capital: Prospects for a new concept. *Academy of Management Review* 27, 1: 17–40.

Alexander, Jeffrey C., and Philip Smith. 1993. The discourse of American civil society: A new proposal for cultural studies. *Theory and Society* 22: 151–207.

Argyle, Michael. 1986. Rules for social relationships in four cultures. *Australian Journal of Psychology* 38, 3: 309–18.

Argyle, Michael, J. A. Graham, and P. White. 1979. The rules of different situations. *New Zealand Psychologist* 8: 13–22.

Bearden, William O., Richard G. Netemeyer, and Jesse E. Teel. 1989. Measurement of consumer susceptibility to interpersonal influence. *Journal of Consumer Research* 15 (March), 473–81.

Becherer, Richard C., Diane Halstead, and Paula Haynes. 2003. Marketing orientation in SMEs: Effects on the internal environment. *New England Journal of Entrepreneurship* 6, 1: 13–22.

Belk, Russell W. 1988. Possessions and the extended self. *Journal of Consumer Research* 15 (September): 139–68.

Brown, Jacqueline Johnson, and Peter H. Reingen. 1987. Social ties and word-of-mouth referral behavior. *Journal of Consumer Research* 14 (December): 350–62.

Burt, Ronald S. 1987. Social contagion and innovation: Cohesion versus structural equivalence. *American Journal of Sociology* 92 (May): 1287–335.

Childers, Terry L., and Akshay R. Rao. 1992. The influence of familial and peer-based reference groups on consumer decisions. *Journal of Consumer Research* 19 (September): 198–211.

Chung, Ed. 2000. Navigating the primordial soup: Charting the lived worlds of the migrant consumer. *Journal of Consumer Marketing* 17, 1: 36–54.

Chung, Ed, and Eileen Fischer. 1999a. Embeddedness: Socialising the 'social' construction of ethnicity. *International Journal of Sociology and Social Policy* 19, 12: 34–55.

__________ and __________. 1999b. It's who you know: Intracultural differences in ethnic product consumption. *Journal of Consumer Marketing* 16, 5: 482–501.

Coleman, James S. 1988. Social capital in the creation of human capital. *American Journal of Sociology* 94 (Suppl.): S95–S120.

Cook, K. S., and J. M. Whitmeyer. 1992. Two approaches to social structure: Exchange theory and network analysis. *Annual Review of Sociology* 18: 109–27.

Donthu, N., and J. Cherian. 1992. Hispanic coupon usage: The impact of strong and weak ethnic identification. *Psychology and Marketing* 9, 6: 501–10.

Dunne, Patrick M., and Robert F. Lusch. 2005. *Retailing,* 5th ed. Mason, OH: South-Western.

Emirbayer, Mustafa, and Jeff Goodwin. 1994. Network analysis, culture, and the problem of agency. *American Journal of Sociology* 99, 6: 1411–54.

*Entrepreneur Magazine.* 2003. Urban, minority entrepreneurs are hotter than ever—so where is their funding?" September 2003.

Europa. 2003. Conference on ethnic entrepreneurship, Brussels. 26 June 2003. http://europa.eu.int/rapid/pressReleasesAction.do?reference=SPEECH/03/353&format=HTML&aged=0&language=EN&guiLanguage=en visited on April 13, 2006.

Fischer, Claude S. 1982. What do we mean by 'friend'? An inductive study. *Social Networks* 3: 287–306.

Frenzen, Jonathan K., and Harry L. Davis. 1990. Purchasing behavior in embedded markets. *Journal of Consumer Research* 17 (June): 1–12.

Gatignon, Hubert, and Thomas S. Robertson. 1985. A propositional inventory for new diffusion research. *Journal of Consumer Research* 11 (March): 849–67.

Glazer, Nathan (1954/c.1964). Ethnic groups in America: From national culture to ideology. In Morroe Berger, Theodore Abel, and Charles H. Page, eds. *Freedom and Control in Modern Society*. New York: Octagon Books, 158–73.

Gnyawali, Devi R., and Ravindranath Madhavan. 2001. Cooperative networks and competitive dynamics: A structural embeddedness perspective. *Academy of Management Review* 26, 3: 431–45.

Gould, Roger V. 1991. Multiple networks and mobilization in the Paris commune, 1871. *American Sociological Review* 56 (December): 716–29.

Granovetter, Mark S. 1973. The strength of weak ties. *American Journal of Sociology* 78, 6: 1360–80.

__________. 1982. The strength of weak ties: A network theory revisited. In Peter V. Marsden and Nan Lin, eds., *Social Structure and Network Analysis.* Beverly Hills, CA: Sage, 105–30.

__________. 1985. Economic action and social structure: The problem of embeddedness. *American Journal of Sociology* 91, 3: 481–510.

Ho, Violet. 2005. Social influence on evaluations of psychological contract fulfillment. *Academy of Management Review* 30, 1: 113–28.

Industry Canada. 2005. Small business financing profiles: Visible minority entrepreneurs. http://strategis.ic.gc.ca/epic/internet/insbrp-rppe.nsf/en/rd01127e.html visited on April 14, 2006.

Inkpen, Andrew C., and Eric W. K. Tsang. 2005. Social capital, networks, and knowledge transfer. *Academy of Management Review* 30, 1: 146–65.

Ireland, R. Duane, Christopher R. Reutzel, and Justin W. Webb. 2005. From the editors: entrepreneurship research in AMJ: What has been published, and what might the future hold?" *Academy of Management Journal* 48, 4: 556–64.

Johnson, Graham E. 1992. Ethnic and racial communities in Canada and problems of adaptation: Chinese Canadians in the contemporary period. *Ethnic Groups* 9: 151–74.

Klandermans, Bert, and Dirk Oegema. 1987. Potentials, networks, motivations, and barriers: steps towards participation in social movements. *American Sociological Review* 52: 519–31.

Kwong, Julia. 1984. Ethnic organizations and community transformation: The Chinese in Winnipeg. *Ethnic and Racial Studies* 7, 3: 374–86.

Light, Ivan, Georges Sabagh, Mehdi Bozorgmehr, and Claudia Der-Martirosian. 1994. Beyond the ethnic enclave economy. *Social Problems* 41, 1: 65–80.

Liu, William T., and Robert W. Duff. 1972. The strength in weak ties. *Public Opinion Quarterly* 36: 361–6.

Mahajan, Vijay, Eitan Muller, and Frank M. Bass. 1990. New product diffusion models in marketing: A review and directions for research. *Journal of Marketing* 54 (January): 1–26.

Masurel, Enno, Peter Nijkamp, and Gabriella Vindigni. 2004. Breeding places for ethnic entrepreneurs: A comparative marketing approach. *Entrepreneurship & Regional Development* 16 (January): 77–86.

McAdam, Doug, and Ronnelle Paulsen. 1993. Specifying the relationship between social ties and activism. *American Journal of Sociology* 99, 3: 640–67.

McKay, Ruth B., and Ed Chung. 2005. Benchmarking for entrepreneurial survival: Pursuing a cohesive and imperfectly imitable culture. *Benchmarking: An International Journal* 12, 3: 207–18.

Midgley, David F., and Grahame R. Dowling. 1993. A longitudinal study of product form innovation: The interaction between predispositions and social messages. *Journal of Consumer Research* 19 (March): 611–25.

Minority Business Statistics. U.S. Commercial Service, sourced at http://www.buyusa.gov/globaldiversity/minoritystats.html?print=1, visited on November 30, 2005.

Oliver, Pamela. 1984. If you don't do it, nobody else will: Active and token contributors to local collective action. *American Sociological Review* 49 (October): 601–10.

Peng, Mike W. 2001. How entrepreneurs create wealth in transition economies. *Academy of Management Executive* 15, 1: 95–108.

Pohjola, A. 1991. Social networks—Help or hindrance to the migrant? *International Migration* 29, 3: 435–43.

Portes, Alejandro. 1984. The rise of ethnicity: Determinants of ethnic perceptions among Cuban exiles in Miami. *American Sociological Review* 49 (June): 383–97.

__________, and Julia Sensenbrenner. 1993. Embeddedness and immigration: Notes on the social determinants of economic action. *American Journal of Sociology* 98, 6: 1320–50.

Rogers, Everett M. 1976. New product adoption and diffusion. *Journal of Consumer Research* 2 (March): 290–301.

Rosenthal, Naomi, Meryl Fingrutd, Michele Ethier, Roberta Karant, and David McDonald. 1985. Social movements and network analysis: A case study of nineteenth-century women's reform in New York State. *American Journal of Sociology* 90, 5: 1022–54.

Rutherford, Matthew, and Sharon Oswald. 2000. Antecdents of small business performance. *New England Journal of Entrepreneurship* 3, 2: 21–34.

Sirsi, Ajay K., James C. Ward, and Peter H. Reingen. 1996. Microcultural analysis of variation in sharing in causal reasoning about behavior. *Journal of Consumer Research* 22, 4: 345–72.

The State of Minority Business. 2001. U.S. Department of Commerce Minority Business Development Agency, sourced at http://www.mbda.gov/documents/stateofminortybusinesses-2001.pdf, visited on November 30, 2005.

Stryker, Sheldon. 1968. Identity salience and role performance: The relevance of symbolic interaction theory for family research. *Journal of Marriage and the Family* 30 (November): 558–64.

Survey of Business Owners. 2002. U.S. Census Bureau, sourced at http://www.census.gov/csd/sbo/index.html, visited on November 30, 2005.

Tienda, Marta, and Rebecca Raijman. 2004. Promoting Hispanic immigrant entrepreneurship in Chicago. *Journal of Developmental Entrepreneurship* 9, 1. Sourced at http://www.findarticles.com/p/articles/mi_qa3906/is_200404/ai_n9379789/print visited on November 29, 2005.

Tilly, Charles. 1978. *From mobilization to revolution.* Reading, MA: Addison-Wesley.

__________. 1990. Transplanted networks. In Virginia Yans-McLaughlin, ed., *Immigration Reconsidered: History, Sociology, and Politics*. New York: Oxford University Press, 79–95.

Toussaint-Comeau, Maude. 2005. Self-employed immigrants: An analysis of recent data. Chicago Fed Letter, No. 213, sourced at http://chicagofed.org/publications/fedletter/cflapril2005_213.pdf visited on April 16, 2006.

*USA Today.* 2002. Asian business owners gaining clout. February 27.

Venkatesh, Alladi. 1995. Ethnoconsumerism: A new paradigm to study cultural and cross-cultural consumer behavior. In Janeen Arnold Costa and Gary J. Bamossy, eds., *Marketing in a Multicultural World.* Thousand Oaks, CA: Sage, 26–67.

Wang, L. Ling-Chi. 1991. Roots and changing identity of the Chinese in the United States. *Daedalus* 120, 2: 181–206.

Ward, James C., and Peter H. Reingen. 1990. Sociocognitive analysis of group decision making among consumers. *Journal of Consumer Research* 17 (December), 245–62.

Weimann, Gabriel. 1983. The strength of weak conversational ties in the flow of influence and influence. S*ocial Networks* 5: 245–67.

## About the Authors

**Ed Chung** (chunge@etown.edu) is associate professor of marketing at Elizabethtown College, Elizabethtown, Pennsylvania. A Ph.D. graduate of York University's Schulich School of Business, he teaches marketing and management and actively publishes in those areas. Some of his recent publications have appeared in *Management Decision, Benchmarking: An International Journal,* and the *International Journal of Sociology and Social Policy.*

**Kim Whalen** (whalenk@etown.edu) is a graduate of Elizabethtown College, where she worked on research projects with Dr. Chung. Her recent work on celebrity endorsement was presented at major national conferences, and a key extension of the work will be presented at the Atlantic Marketing Conference.

# *From the Practitioner's Corner*
# The Often-Neglected Term in the Entrepreneurial Equation—the Purchase Order

Deaver Brown
Joseph E. Levangie

*Many entrepreneurs are enthralled with their company's technologies, products and potential markets. Invariably these emerging ventures present bedazzling business plans with industry-wise vernacular, detailed market research, and sophisticated financial spreadsheets. They often flaunt their "optimized business models." Investors, however, typically want to know when and how the sales will start meeting the Plan. "Where's the purchase order?" is the refrain. In this article, our "Practitioner's Corner" associate editor Joe Levangie collaborates with a long-time colleague, Deaver Brown, to address how businesses should "make sales happen." Levangie warns that Brown's elitist education (Choate, Harvard College, Harvard Business School) should not be interpreted as a lack of "street smarts"; Brown's more entrepreneurially friendly credentials include winning Golden Gloves boxing medals and selling Fuller Brush products door-to-door! To ascertain how the entrepreneur can wrest an order from a prospective customer, read on.*

The old adage is that "If you build a better mousetrap, the world will beat a path to your door." Don't bet on it! The reality is that the New Venture trash heap is piled high with cratered entrepreneurial initiatives that failed from sales shortfalls. Most entrepreneurial research studies suggest, however, that "lack of capital" is the overwhelming reason for business failure. This is true. But a closer look at the financial dynamics of the typical venture underscores the need for sales success: sales revenues generate gross profits (sales net of materials and direct labor) which help absorb company expenses, thus extending the venture's cash reserves. Investors, banks, and BODs encourage the conservation of cash! While it is ultimately the lack of cash that sinks a business, sales generation (early and often) can keep the doors open during the critical early stages of the venture and create an operational platform for profitable growth.

Let us examine the root cause of the success (and failure) in the entrepreneur's quest to generate sales:

- Where does an entrepreneur go to learn about selling?
- What are the requirements for sales leadership?
- What are the elements of building a winning sales team?
- What kind of "selling culture" needs to be established?
- What is the nitty-gritty of actually getting a purchase order?
- What lessons can be gleaned from real-world experiences?

## Desperately Seeking the "Sales Mystique"
### *What Do the Traditional Sources of Advice to the Entrepreneur Provide in the Area of Sales Techniques and the Generation of Purchase Orders?*

Disappointingly little has been published to assist entrepreneurs unlock the key to the sales mystique—that epiphany that may come to the entrepreneur and lead to success in closing sales contracts with customers. For aspiring entrepreneurs weaned from the safety net of a big company or thinking that a purchase order is akin to a government R&D grant award, the need for an injection of selling acumen is clearly present. Over the past two decades, the two authors have collectively interviewed hundreds of entrepreneurs and assisted them launch dozens of successful companies. More importantly, each author has been an active and serial entrepreneur, setting up several new and successful enterprises. Most entrepreneurs whom they have observed have displayed extraordinary capabilities in the areas of engineering design, strategic planning, "big-picture" strategic marketing, manufacturing, and finance. Often, however, selling competence is not part of the skill set. One-on-one counseling on selling from seasoned veterans is most helpful. It is not often available. Absent such hand-holding, these aspiring venturers have sought out written knowledge on the ABCs of selling.

Where might one direct these entrepreneurial wannabes? Practical "selling help" for the entrepreneur from conventional sources is, regrettably, difficult to obtain, as reflected by the following sampling of references many entrepreneurs routinely use:

- *American Management Association (AMA)*. The marketing management section of the AMA produced a classic text, *The Marketing Mystique* (McKay 1972), in which the author tried to defuse the "aura" of marketing. The objective was to persuade businesses to adopt a marketing concept that compelled them to be more customer-friendly. The five marketing tasks recommended were

1. development and maintenance of a marketing-oriented attitude and philosophy;
2. structuring and staffing of an effective organization;
3. initiation and conduct of strategic planning;
4. managing of a dynamic operating system; and
5. appraisal of marketing performance.

This AMA classic—useful for marketing guidance to the entrepreneur—never addresses, however, even the notion of a purchase order!

- *The Smaller Business Association of New England (SBANE).* SBANE produced a *Start-up Guide* (Hexner 1987) which included informational resource references for
  - strategic planning assistance;
  - legal and audit professional services;
  - BOD and other advisers;
  - marketing and product development guidance;
  - funding sources; and
  - government assistance.

This is a practical and most helpful entrepreneurial aid, but again, nary a word about selling and getting purchase orders!

- *How-to Book 2005* (Banks 2005). *The Boston Business Journal* produces an annual reference book for regional businesses and entrepreneurs that includes contact information in the following areas:
  - legal, audit, engineering, and construction;
  - VCs, banks, and SBA loans;
  - staffing and temp help;
  - education, training, and motivational speakers; and
  - sales training.

This is a great regional resource for small businesses, but has only one obscure reference to selling (sales training). Enrolling in a sales training course might get the entrepreneur closer to understanding how to secure a purchase order, but most entrepreneurs do not have the time or inclination for training courses.

### *With the Exception of Actually Taking Sales Training Courses, the Notion of Unlocking the "Sales Mystique" Remains a Mystique; Are There any Readily-available Hands-on Resources to Help the Inquiring Entrepreneur Better Understand Selling?*

Obviously there are many books on sales management. Few of these have the entrepreneur in mind. There are, however, two entrepreneurial books well-known to the authors. Baty (1990), in his *Entrepreneurship for the Nineties,* has a chapter (1 out of 30) devoted to "selling" that addresses market research, pricing, PR/advertising/product literature, rep networks, and international marketing. While there is little discussion of selling techniques and buyer psychology, Baty does convey a useful message. He opens the chapter with: *"Nothing happens until you get a purchase order."* He closes with, *"Sell, sell, sell!"*

Coauthor Brown is particularly fond of *The Entrepreneur's Guide* (1980), a seminal reference he wrote a quarter of a century ago and is in its 18th printing as a book and 50th as a CD. All aspects of Brown's selling advice are still relevant today; key points are included in this article. Here's a sample:

> As a young man, I thought it was obvious that you had to know your deal. I learned that early as a Fuller Brush salesman. You had 30 seconds to get their attention; if you did, fine. If not, move on. I got to refine my pitch 50 times a day; I refined it so I made a lot of money. Most salespeople do not have that training in the beginning and do not realize they have just that 30 seconds in every sales situation.

### *Is It Ever Too Late for the CEO-Entrepreneur to Unlock the "Sales Mystique" and Become More Customer-oriented?*

Not if the entrepreneur is still alive and breathing! Not even if the venture is an unqualified winner. Consider the case of Nike's Phil Knight. In an interview (Willigan 1992), this outstandingly successful CEO-entrepreneur admitted, "We used to think everything started in the lab. Now we realize that everything spins off the consumer. And while technology is still important, the consumer has to lead innovation. We have to innovate for a specific reason, and that reason comes from the market. Otherwise, we'll end up making museum pieces."

## The Entrepreneur as a Sales Leader

### *Where Does the Entrepreneur Start in Introducing a Selling Concept to the Venture?*

The best sales team usually wins in business. In new ventures, the sales task must start with the entrepreneur who may also serve as the sales team's quarterback. The toughest position to hire for is the lead salesperson. Why not do it oneself? Anecdotally, it seems that more than 90 percent of successful new ventures have the CEO-entrepreneur as the lead salesperson for key accounts.

When Brown wrote *The Entrepreneur's Guide,* after selling his Umbroller Stroller company (Cross River) to Rubbermaid in the late 1970s, he determined that the characteristic considered most crucial for new venture success was the sales skills of the CEO-entrepreneur and his or her willingness to employ them on a daily basis.

Selling is not a job that can typically be delegated successfully. The successful entrepreneur, therefore, must often start the selling process by looking in the mirror.

### *Why Is Entrepreneurial Leadership in Sales So Important?*

The CEO-entrepreneur can provide executive-level attention and weight to key customer relationships. In contrast, established "Big Company" competitors generally cannot. These more "structured" companies have probably delegated the sales function down the ladder in their organization so that their leaders can concentrate on "more important things"—such as endless internal corporate meetings!

T. Wilson, the legendary CEO of Boeing who transformed the company into a worldwide leader in aircraft sales, when asked, "What he was," used to say, "I am a plane salesman. Why you may ask? Because if I sell a lot of planes, people *like* me; if I don't, they *don't.*"

Edwin Land of Polaroid, Bill Gates, and Ken Olsen of Digital Equipment positioned themselves in their respective markets as an "inventor," a "nerd," and an "engineer." They were, however, consummate *salespeople.* Neither Polaroid nor Digital generated much excitement after the two founders retired. Microsoft lost its mojo when the legendary Gates took a backseat.

What did these renowned entrepreneurs do to provide selling leadership?

First, these larger-than-life personalities were always entertaining and quotable. Land regaled his annual sales and shareholder meetings with his stories, inventions, and ideas; everyone looked forward to them, much as they do for the Warren Buffett extravaganzas of the present day (guess where Warren got the idea?). Land's prices for cameras and film were always somewhere between excessive and totally outrageous—but no matter. The purchase orders rolled in.

Olsen ragged salespeople up and down as he emphasized that "only" the engineering mattered. Of course, Olsen was selling to the best of all possible customers—other engineers. These kindred techno-spirits lapped it up and idolized him! He got his price, and closed on huge orders in the process!

Gates doggedly pursued day-to-day sales activities, with a dash of aggressive pricing. He essentially "encapsulated" the purchase order in the Microsoft operating system included in most personal computers sold, and became the world's richest man.

Sam Walton had a similar charisma. When George Bush Sr. went to Bentonville to present "Mr. Sam," as Wal-Mart people called him, with the National Medal of Honor, he could not believe the love and support of those Wal-Mart people for their leader. "Selling leadership" extends to selling the employees!

The authors have each (separately) had the opportunity to talk to or to meet each of the aforementioned celebrity-entrepreneurs. They were appropriately wowed by these entrepreneurial legends. Everyone in their presence basically took a ticket and got in line. And, as with so many other great leaders, to this day the authors still revel in telling people about these encounters with these leaders "who could close the deal." Wonderful…something out of the ordinary in a very ordinary world…and that is the key to why entrepreneurs must sell—*to make an ordinary day special and different for the buyer.* The ongoing flow of purchase orders is the natural consequence of executing the selling process correctly.

### *Why Do So Many Entrepreneurs Fall Short in Getting a Purchase Order?*

Shortcomings in generating purchase order flow stem from a variety of entrepreneurial frailties, including

- lack of understanding the customer;
- confusing "hard work" with achievement;
- poor sales technique; and
- bad time management.

Salespeople who fall short of their quota in closing on purchase orders often provide a litany of *excuses* for unsuccessful customer interactions. Among their reasons are

- The customer was out of the office.
- We ran out of time in the meeting.
- They want us to tweak our design (or packaging or literature).
- They were my last call and I was running late.
- They want to take another look at their inventories.
- There simply was bad chemistry.
- Our pricing is too high.
- I think the buyer is in our competitor's camp.
- It's not clear who's calling the shots.
- I never got around to asking for the order!

As George Boule has written (Goodman 1997), "Salesmanship starts when the customer says no."

### *How Should the Strategy and Tactics of Selling Evolve to Avoid Such Shortcomings?*

Most salespeople are burdened with a complex mission. Overlay the workload of the entrepreneur, and focus can indeed be difficult. Think of the mission as a battle plan. The excessively ambitious CEO-entrepreneur often has too many contradictory other missions in mind (IPO opportunities, new products, siting a new plant, patent applications, etc.). Any one or two might be doable, but the third and fourth complicate the end game, dilute the resources, and create the undoable task. For a simple image, consider Hitler as CEO. His despicable particulars aside, he perhaps could have beaten the British, the Russians, or conquered North Africa. He might have been able to do two of three of these missions. He tried, but could not do all three. His ultimate fate, of course, was the equivalent of the entrepreneur filing for Chapter 7!

When devising the sales mission, be sure it is a *doable task.* The flaws of talented entrepreneurs are often to try for too much. Remember, while entrepreneurs may know this reality, they may never admit it. This is especially a problem for the small business leader who must both devise the sales plan and implement it. The entrepreneur is the player and the referee, all in one mixed bag. So the entrepreneur must work very carefully not to overburden the tactical plan with too much strategic complexity. Pick goals consistent with existing (or contemplated) resources.

This practical approach to strategizing seems a simple matter in retrospect. Yet as the great UCLA basketball coach John Wooden said upon retirement:

> I always thought it was simple when I was young. I never understood why no one else did it. I looked at my players; I figured out what they could do and not do; and that is the way we played. When we had height, we played to that advantage; when we had speed, we played to that; when we had shooters, we played to that. It was always a mystery to me why so many coaches forced their game plans ("tactics") to fit their personal style ("strategy") when the players just couldn't do it. (Brown 1980)

One of the great problems about learning how to sell is that the great salespeople just do it and don't think much about how they do it. This is one reason the great hitters such as Ted Williams and Ty Cobb could never coach. Swinging a Louisville slugger was so natural to them that they could not understand why everyone could not do it.

The challenge is to dissect the problem and concentrate on what works. This is why so many coaches happened to have been mediocre (or worse) players. They became students of the game. Their weaknesses permitted them to evaluate; it almost forced them to do so. Our discussions in this article are efforts to get you to think about the process, the opportunity to sell, and the wonderful results if you are successful.

*Tip:* Sales results come from concentration on what's truly important.

### *How Do Real-world Customer Types Impact the Strategy and Tactics of Selling?*

The CEO-entrepreneur who wants to be the leader of the sales team must acknowledge an important reality about selling. It is not just a matter of "you and the buyer." It is a matter of your organization and their organization. There may be a complex decision-making process involved within the customer's organization Consider some of the players who might impact the issuance of a purchase order.

***Economic Buyer.*** This is the budget setter. This person is rarely available to the seller; he or she pulls the strings in the background by setting the general terms of the purchase order in terms of budget and needs.

***The Technical Buyers.*** These are the people who are relied upon to keep the company or buyer out of trouble. They are considered gatekeepers and usually fiercely protect this role. It is a very rare buyer or economic buyer who will cross this person.

***Buyer.*** This is the traditional person most salespeople think makes all the decisions. This person meets with you, but must check decisions with the economic buyer, carrying your message, and then checks it out—voluntarily or involuntarily—with the technical buyer.

***Coach(es)***. This is the person or people who can lead you through all these organizational land mines. This can be everyone from an assistant, receptionist, to the buyer, technical buyer, or economic buyer themselves. Most salespeople spend far too little time cultivating these relationships.

## Building a Successful Sales Team

### *What Are the Issues in Hiring Good Salespeople?*

Much has been written on sales organizations. Throw an entrepreneur into the mix, however, and you have a challenging dynamic. Some entrepreneurs always try to go top-shelf in hiring staff. Others are biased in favor of technologists, but with regard to salespeople are willing to accept mediocrity. To avoid such potential mediocrity, consider hiring salespeople as follows:

1. *Hire someone experienced in your industry without too many biases about the market.* Of course, this statement has an inherent contradiction since all people in an industry have built-in attitudes and biases. There are several ways of getting around it. When coauthor Brown's company Simply Media was looking for a key account salesperson, it was decided to go after someone familiar with consumer products since Simply Media's products were sold as consumer entertainment, not software. Former computer salespeople, who would probably had been previously trained to overdemo, were avoided.
2. *Be alert and interview recently fired salespeople from your competitors.* Salespeople tend to be terrible politicians; many of them talk too much, sell too

much, and their bosses want them out of the way. Occasionally the bosses succeed. Look for these people; the good ones are jewels. At the Umbroller Stroller company the best salesperson had been fired by its largest competitor; at American Power, the new CEO had been terminated by his old company, had terrible references from several disgruntled venture capital groups, and was the perfect person to lead the company to more than $2 billion in sales. Successful entrepreneurs and salespeople typically learn from their mistakes.

3. *Watch out for "marketing people" who are trying to sneak into your company.* Marketing people know that you actually need salespeople; often they have the ability to do sales, but never will. They hope to sneak in, then move to another "more appropriate" position. Watch out for these people; they can outfox you.
4. *Look for "nice people" who are aggressive self-starters.* Niceness is sometimes overlooked in the set of skills recommended for good salespeople. Look for these traits in others. But be sure they are more than superficially nice!
5. *Look for people who don't like to sit down for too long.* Good salespeople keep moving. Marketing people get too comfortable in their leather-cushioned lounge chairs. You need people who want to go on to the next call, the next customer, the next deal. As a result, they have to close the sale to move on out. You want these people.
6. *Hire people who really, really like to sell.* While most competent entrepreneurs look at selling as a necessary evil, there are some selling "idiot savants" who get endorphin highs from closing the deal and walking away with the purchase order. As reported by Exley (1993), sales guru John Fenton has exclaimed, "Selling has to be the most exciting thing you can do with your clothes on."

### What about the Folklore of Superstitious Salespeople?

The folklore is often a reality. Gellerman (1990) reported on an observational study he performed on 25 salespeople. He found that almost all the salespeople were convinced that there were good days for selling and that there were bad days, and that the outcome was basically predetermined (at the whim of the sales angels?)! "Furthermore, they maintained that they could usually tell what kind of day was in store for them after their first few calls," noted Gellerman. Of course, such thinking is confusing cause with effect, can be self-fulfilling, and sometimes is self-defeating. Early-in-the-day success can be uplifting and may bring out the best in the salesperson—confidence, attitude, adherence to the selling fundamentals, etc. Conversely, early-in-the-day failure can be depressing, bruising the ego and confidence of the less competent salespeople. Selling is a tough way to make a living, and the salesperson's ability to manage rejection will help determine success.

### What about the Sales Manager Who Must Tend to These Salespeople?

The most productive sales manager for an entrepreneurial organization tends to be a nuts-and-bolts individual, suspicious of the chaotic, zealous new enterprise environment. The sales manager's natural inclination will be to bring order to the confused new enterprise. These individuals rarely share the entrepreneurial goals of deferred compensation, and well-paid retirement. They generally prefer immediate income gratification and a substantial expense-account budget as rewards for their achievements. These traits conflict significantly with the entrepreneur's hard-work ethic and long-range dreams. Despite the potential for personality clashes, the entrepreneur needs a nuts-and-bolts individual to manage the sales organization and bring in the purchase orders.

The really good sales managers try to understand their people. As GE's retired CEO legend Jack Welsh recommends (Collingwood and Coutu 2002):

> Get into the skin of every person so that they know that their ideas count. Celebrate small successes. Evaluate the people down to the lowest units, so they know that they count. It's critical that people know their achievements are constantly being measured and that they count. It's critical that people know that their contributions matter. It's critical that they know that they will be seen and rewarded.

### What About Reps?

Early on, many new ventures cannot afford full-time salespeople. As a result, companies often turn to independent sales agents known as manufacture's representatives. They are paid strictly on a variable commission basis and therefore do not represent a fixed overhead burden to the venture. Reps also benefit the new enterprise by providing experienced sales coverage and bringing strong customer relationships to the venture. Most reps carry several lines and really don't have to follow the entrepreneur's directions. As the company's line becomes more important to the rep, this problem lessens, and benefits to the company accrue.

### What Are the Mechanics of Selling?

The mechanics of selling should be perfected to improve your effectiveness. Most people generally underrate these procedures because they are seemingly so routine. Do not make this mistake. Here are field-tested suggestions on selling mechanics (with an emphasis on retail channels) from co-author Brown.

1. *Create a database.* Every salesperson needs a well-developed prospect and customer list. The first step is to learn to use a computer and use a sales contact program such as ACT!. You can store a variety of different lists (customer type, industry category, product developments, etc.) should your industry or area of responsibility change.

   Keep the old contact list, however. People have a way of resurfacing elsewhere. Interestingly, when you meet someone in a new situation, even a modest contact in the "old place" may make you seem much closer in the new one. This has happened to entrepreneurs many times. There is a wonderful New England expression for this phenomenon, "It isn't how well you know someone, but how long." Old contacts make for great door openers.

   There are essentially two kinds of buyers: (1) those who are paid to see you (e.g., retail or industrial buyers who are paid to see vendors and potential vendors); and (2) those who are not (e.g., individuals such as those to whom car or insurance salespeople sell). Retail and industrial buyers can be identified by various trade books such as Chain Age, Thompson, and other related periodicals. Another way to build a database is to enter names from trade periodicals in your field. If you do this for just 12 months, you will build up a surprisingly good file.

   Keep particularly alert for the top 50 to 150 accounts in your territory. This territory can be as small as a neighborhood of a city and as large as a worldwide list. Given the 80/20 rule, which is really 95/5 (i.e., 95% of your results come from just 5% of your customers), you should always be on the lookout for new customers that can make your top 50 to 150 accounts.

   In addition to the ACT! contact file, keep a customer clippings file. Any news or important events that includes quarterly results, if they are public company, should be retained. Get their annual reports if they are publicly traded. This attention to detail can pay off in getting your selling proposition, or your deal, in harmony with the business plans of your customer. If the customers are trying to increase margins, you can craft your product offering accordingly; if they are trying to increase sales, you can suggest promotions.

2. *Getting appointments.* Getting appointments with buyers paid to see vendors is relatively easy. You need to have a 30- to 60-second speech prepared as to why they should see you; in the contact stage, do not try to sell them on your product or service, just on seeing you. Keep at it; do not leave messages; just keep on calling until you secure an appointment.

   When first contacting customers, make it easy for them. Meet them when and where they want. Do not start by trying to get them adapt to your schedule—unless you believe this is the only way to get them to see you (i.e., "I will be in your area-town-city on a given date, can you see me at 10AM?").

   Keep your top accounts on a limited mailing list that keeps your products or services in front of them on an ongoing and updated basis.

*Tip:* If you want to reach the key customer contact, try before 9AM and after 5PM, which are often the best times. They are not expecting cold calls then; if they have gatekeeper secretaries these zealot impeders are usually not there then.

3. *Practice your two-minute presentation.* You must have your own deal down cold so you can respond to the customers' questions or interruptions. If you really understand your own deal, you can answer responsively, encourage their participation, let the conversation wander or evolve, and still close the sale. Very few salespeople know their deal; if you keep practicing the pitch on customers, you will find out what works and keep it; what doesn't and drop it; and what intrigues them and build on it.

4. *Carry a big sales bag.* Brown learned long ago to bring the big, bulky sales case to key customer meetings. That way it showed "I am serious," and not just another executive with a skinny elegant briefcase full of nothing. The symbolic value is important; it says, "You are serious; I have all the stuff with me."

   In your sales bag, make sure you indeed have all the right stuff: price lists, catalogs, customer support documents, necessary forms to set up a listing, and documents required to be filled out for the sale.

   If they say "yes," you want to be able to close. While most salespeople do not have the sales closing documentation, make yourself the exception. On a human note, buyers appreciate salespeople with the information. The number one complaint of most buyers is salespeople do not have the information. Astound them; bring the stuff.

5. *Respect the customers' time.* Do not take more than 30 minutes. As has been said to several buyers, "We are not selling Boeing 747s here." The implication is this is a simple, straightforward doable deal. This makes them relax; the longer the presentation takes, the more worried most buyers get. After respecting their time, tell them, "I am glad we could do this quickly so we did not use too much of your time."

They will appreciate the thought and remember you well for it.

*Great Salesperson Story.* When new long distance telephone services were coming out, many people tried to sell entrepreneurial businesses. Brown observes, "They never had the stuff, the details, the facts. One salesperson called and said he would take 10 minutes; when he arrived I took out my watch and said, "Go." At the end of 10 minutes he had sold me, completed the paperwork thanked me, and left. I just had to call his office and find out more. Yes indeed, this rather modest, quiet person was their number one salesperson. Naturally, I asked the office boss why. He gave me a bunch of reasons that really had nothing to do with it. The reality was that the man was quick-fast, modest, easy, and made the whole process seem natural. Speed, speed, speed. It is a great way to close."

6. *Appearance and manners.* Suits are the usual uniform. Sports jackets are okay in the more informal parts of the country. Be neat; orderly; quiet. Sit where they want you to; do not ask them a lot of questions. No jokes. No one can tell a good joke; even Jay Leno has a hard time connecting every time. Stay away from the yucks. If you are selling to women, do not move in on their personal space; this applies just as much to both male and female salespeople.

   Tell them why you are there; tell them when you will leave by; and be straightforward. Do not say anything to a new prospect that you would not say to your own grandmother. Miller (1986) noted that the great salespeople tend to be quiet on the sales call even if they are loud and talkative outside of that environment.

7. *Telemarketing.* If you are in the telemarketing sales business, this is an entirely different kind of selling and should be approached that way. A number of books have been written on the subject; an inquisitive entrepreneur might sign up for at least one seminar with AT&T or the local phone company.

*Tip:* When telemarketing is part of the sales process, remember that the prospect cannot see you. Use this to have all your notes and information spread out in front of you. The best telemarketing people have notebooks with sections key coded for objections such as "College-Aged children." So, if a prospect says, "I have college-aged children so…." the salesperson flips to the section that lists the benefits for that group.

8. *Be organized.* The image of the bungling salesperson is a stage prop in the movies and on TV. Great salespeople are absolutely the opposite. In fact, they are usually quite graceful. This makes sense if you think about it; no one wants a bumbling fool stumbling around their office, home, or personal space when you are out of the house. Your sales practice should include how to enter a room gracefully, present your materials, and withdraw when the meeting is over.

*Tip:* For every sales call, I prepare a short, tight presentation that I have out when I enter the office. My sales bag has the rest. This way I do not have to open the bag, pull out the papers and samples, and have the buyer watch me fumble around. Always have an order pad with the forms, and two pens with you (one might not work, and you always want to give the customer a pen with the paperwork).

9. *Start your day early.* The best salespeople get to work early, do their preparation in the morning, and leave at a reasonable time. They set up their key appointments for the morning; are wary of late-afternoon appointments; and do not overschedule themselves.

   Starting the day late is like trying to chase a train out of the station. You have to run faster and faster just to stay even with the train as it roars away. An early start lets you get prepped for the day. First you plan the work then you work the plan. If you start late, you have to do this out of order; plan the work and then work it the next day. Late salespeople who try to struggle with their paperwork at the end of the day when they are tired always have a feeling of "being behind." Get over it. Get to work early. Period. If you are on the road, schedule your first meeting as early as possible. Most productive selling work is done before 2PM. After that, most sales calls are just spinning your wheels—unless this is the only time they will meet you. Some nasty buyers schedule you for 4PM on Friday, just to test you. Meet the challenge; see them. But avoid setting future meetings for those times.

## Creating a Winning Sales Culture

### *If Setting Up a Sales Organization Is Relatively Straightforward, Why Don't More Entrepreneurs Implement a Company Culture that Nurtures "Selling?"*

Some CEO-entrepreneurs are going out front and leading the sales effort. The problem is that not enough are seizing the reins and doing it. That is why we need to continue to preach the Gospel of Selling in the attempt to convert a few more people! Instilling a winning sales culture requires, we would suggest, an understanding of societal issues such as work, relaxation, wealth, and respect.

We might reach back to the 19th century and Thorstein Veblen's (1899, 1970) *The Theory of the Leisure Class.* The essence of elegance, as defined by society, was to do and own useless things to demonstrate that you were above the scramble of the everyday hardscrabble life. In other words, you chose your hobbies, such as exercise, because you had too much food, too rich a life, and too much in general. You could get the same exercise by doing yard work, but that would be a "useful" activity and identify you as "having to do it."

Golf is a similarly respected activity. It takes a great deal of leisure and money to play a round of golf. Only those blessed with both time and money can do so; especially respected are those lucky few who can do it during the workday. Few people seem to comment on the fact that golfers generally spend their time on the course cursing their swing, the lie of the ball, their clubs, and their luck. Golf can be more work than the job itself; it is certainly more frustrating for most people than their jobs. Yet, few will admit that reality.

Some entrepreneurs—when they can spare the time—enjoy the game of golf as long as it remains that—a game. Yet one notices that most golfers take the game as seriously as anything else in their life. Each bad shot can become their particular crisis. They often don't seem to be having "fun," as one normally defines it. So why, one wonders, do they do it?

This golf metaphor provides an interesting conundrum for the prospective salesperson to consider: How to work on getting beneath the surface of things to understand people's true motivations. The ability to draw such insight reflects an ability to make the sale.

The premise is that people play golf for many, many reasons because golf is: (1) worthwhile; (2) what true leisure is; (3) part of being successful; (4) good for business; and (5) just something to do. Finding out, for example, why the potential customer likes, or dislikes, golf can provide important clues as to what is important to that person.

According to Veblen, manual work is "disdained" because it is so necessary. Think of where society would be without garbage collectors, dishwashers, phone repair people, and assorted other performers of critical tasks! The "most valued" work, in contrast, is theoretical or removed from specific necessity.

From this viewpoint comes the bias in favor of people aspiring to become professionals, especially professionals who do arcane and generally useless stuff. So, the divorce, probate, and criminal lawyers get little respect because these are mundane and necessary activities; Wall Street lawyers get a lot of respect because they do complicated work that generally has no practical impact whatsoever other than winding up in musty files. Doctors who act as GPs or pediatricians, who we all need, get little respect compared to the fancy surgeons. Marketing people are admired; sales managers are tolerated; but road salespeople are looked down upon even though the business would fold without them. Who wants to be a Willie Loman? See the point? An entrepreneurial culture that ignores those "lowly" salespeople who actually bring in the purchase orders is more than a little dysfunctional. As with most obvious points, they tend to be disregarded.

In many businesses, the sales, production, and customer service people who make stuff (customer service people "make stuff" by communicating with customers) get little respect. "Marketing gurus" and "strategic planners" get the lion's share of the respect. As Tom Peters has often suggested, a sales or customer service person who talks to five people will find out a lot more about customer opportunities than most marketing gurus or strategic planners in their daily routines. The golf analogy would involve talking to the starter or the caddies to get the scoop on the inside stories of the country club! The entrepreneur needs to talk to the *real* workers and the *real* customers! The entrepreneurial culture needs to be biased in favor of the sellers in the organization.

### *What Is Needed to Introduce Sales-oriented Problem-solving to the Entrepreneurial Culture?*

What does all of this analysis have to do with sales? People, people, people; motivation, motivation, motivation; otherness, otherness, otherness. *Not* me, me, me. That's the sales culture the entrepreneur needs.

To sell, the entrepreneur must absolutely think about why people act as they do, not take things at face value. Few people admit that they pay attention to advertising. Yet most routinely buy consumables like Crest toothpaste and think a Rolls Royce is a pretty neat car—despite never having driven in one! The seller must interpret and understand such behavior.

The entrepreneur's challenge is to keep an open mind so that opportunities can flow in. You need to look at things creatively to seize the opportunity and make the sale. How often have you heard salespeople say about the customer: "He had a lot of stupid comments"; "She didn't understand"; "They weren't listening." The real message, of course, is the salesperson was not listening.

*"He had a lot of stupid comments." Message:* The salesperson discounted the customers' points because they were not deemed reasonable or warranted in his or her judgment. *Solution:* Customer objections to sales presentations suggest that something could be learned; something new is going on; this is precisely the time to be listening.

*"They weren't listening." Message:* You turned them off like a light switch. *Solution:* Listen and regroup if they are not paying attention. Find out why. Something is going on; the salesperson just missed it.

*Tip:* Just because you do not understand the customers' feedback does not make them "wrong," "crazy," or "stupid." In fact, if you believe those things, you are the one who is wrong, crazy, and stupid.

### *What Is Needed to Turn the Tables and Pursue Selling from the Customer's Viewpoint?*

Think about your sales situation from the buyer's perspective. A simple thing, usually overlooked, is that most buyers (just think about yourself when you are about to buy something) are most concerned about *not* doing something stupid. They are not as concerned with the right answer as avoiding the wrong one. They are not seeking the ideal answer, but just a reasonable one. Addressing this concern is always of top-most importance.

If you play chess, the perfect approach is to stand up and observe the board from your opponent's point of view. The perspective is startling. The same goes for most sales situations. Consider the sales proposition from the customer's perspective.

Search out the differences between appearances and reality. To sell effectively, you must labor hard on this mission. Think of the simple example of the agreeable prospect, nodding at your every point; then think of another who challenged you sincerely on various points. On the surface, the agreeable prospect "appears" the more likely buyer, but experienced salespeople know that a challenging series of questions from a buyer is a much better prospect.

As a wise professional once observed about becoming an executive or a lawyer, "First learn about *people;* the business or lawyering part will then be a lot simpler." Understanding how people work, and responding to their needs, is how you match the benefits of your product or service to their situation. In simple terms, God gave you two ears and one mouth—good salespeople use them in proportion.

Brown notes, "Many salespeople who have worked for me have commented that I talk at length about selling, the customer account, the prospective orders, and the dynamics of the overall buyer-seller situation. Yet, they notice that I keep it quick and simple with the buyer themselves. The reason is it takes a lot of work to make the presentation simple, clean, and effective. Or, as Franklin Roosevelt once apologized in a letter, "I am sorry this letter is so long; I did not have time to write a short one."

## The Nitty Gritty of Getting the Order

### *Does the Entrepreneur Know His Own "Deal?"*

Consider co-author Brown's personal experience.

> My first real-life explanation of the importance of the "deal" came at The Hardware Show in Chicago during the early 1970s. While covering the booth, I was approached by an elegant looking gray-haired man, with a country boy demeanor, who put a tape recorder in my face and said, "Tell me your deal, kid. You have two minutes.
>
> I did. I got the order. I asked him what was the big hullabaloo, why the tape recorder? He said, "No one knows their deal. Let me show you." So, he put me in tow and we went to other booths and asked the same question. After the sixth failure, he winked at me and said, "See. You'll do fine; just remember your deal. And always pitch it the way you did, from my point of view, not your own."
>
> That was the late, great Sam Walton—when he had only 22 stores.

### *How Does the Entrepreneur Develop a Sales Team with the Right Temperament that Is Presentable, Is Disciplined, and Gives the Customers What They Want?*

As Oscar Wilde once said, "Experience is the name we give our mistakes." He also said that people rarely lament their mistakes. In effect, if and when you made a mistake you were in the game actually *doing something.* It might not have worked; but you were there. It was real, something happened, and you felt real and human.

If you do not share that point of view, and have a glass jaw where one hit knocks you out, sales and entrepreneurship are certainly not for you.

*Tip:* Salespeople are like dogs, kick them and they come back again. Cats are like buyers, one bad look, and they are gone for good. Good salespeople have to be more like dogs than cats.

The best writer on business is arguably Peter Drucker. His book, *Managing for Results* (1964), remains a landmark some 40 years after original publication. He gets most things right. The one area where Drucker may be off-base is his conviction that good managers can be good entrepreneurs. The reality check is that good managers may have skills to be good entrepreneurs—but will they actually take the risk to get into the game? Is their temperament suited for the job? The exact same problem exists in getting people to perform the sales job.

Many people can do sales; but will they? In this case, will the entrepreneur? Does your temperament permit you to do the nitty- gritty job of selling versus the more elegant, but less useful task of managing or marketing? One must deal with this temperament issue before starting to refine other talents. A few key points are worth emphasizing and reemphasizing.

- *You must genuinely like and care about people.* Today, people are experienced and worn out by all the sales pitches and ads machine gunned at them. They have become more skilled in filtering the real from the phony. The first turnoff is if they feel the salesperson or advertiser is not genuine or real.

  Gerstener, former CEO of IBM, and Bill Gates of Microsoft may be busy doing a lot of sophisticated things, but they obviously get a kick out of people. They like to mix it up. Gates even played golf with President Clinton! Gerstener simply loved to talk to people.

In contrast, there are the examples of Palmer and Olsen ex-CEOs of (the former) Digital Equipment, both of whom were known as elite nonsocial types. They did not enjoy mixing with people. Palmer was known as a fashion plate; Olsen as a down-home, red-shirted Maine type. People were not their thing. If they would not sell, they had to let someone else try. The same goes for every entrepreneur. Don't force-fit misanthropes into the selling process!

- *You have to be able to listen and reevaluate based on new information received.* A salesperson is like a waiter who starts out with a menu and comes back with a tailored, individual order. If one diner likes steak and the another chicken, neither one is right or wrong. The same principles apply to dealing with customers; each has particular requirements. These needs are neither right nor wrong. It is especially not the function of the waiter, or salesperson, to pass judgment on customer requirements. Far too many salespeople spend time criticizing the issues raised by buyers instead of addressing them. Instead, they should be linking product benefits with customer needs.

  One reason French restaurants have really never worked in the United States is that Americans do not like to be told what is right and what is not, and to be made to feel foolish because of their choices or suffer the condescending attitudes of the French waiter-type. All too many salespeople come off like French waiters!

- *You should be quick, short, and respect the customers' time.* Nothing is respected by a buyer as much as brief, concise, documented presentations. The number one complaint of buyers is that salespeople do not have the facts. The number two complaint is that salespeople take too long and do not get to the point. Nothing is remembered better than giving buyers the gift of their time back. Just because you have flown 3,000 miles does not mean you should spend a long time on the sales call.
- *Stick to the customers' needs, not to your opinions; knowledge is king.* Keep "I" out of your presentation and put "you" in. This is not trivial. Learn their business; understand how your products or services could better their situation. Tailor your presentation accordingly. Some might view this as phony. Buyers acknowledge that, yes, this is an obvious tact; but they also state that it is all too rare and the salespeople who do bother to scout the territory always make better recommendations. In other words, it is a blunt, bolder approach; but it works for both sides.
- *Do not interrogate the customer. Do your research in advance.* If you have questions, call the library. The buyer should not be subjected to cross-examination. It is *not* the inalienable right of the salesperson to ask or the requirement of the buyer to answer. Questions usually frustrate and irritate the buyer; most want to just say, "Tell me your deal and get on with it." This advice is contrary to most sales advice. Most of that advice relates to trapping buyers with questions. Bad idea; overused. Good salespeople do not need it.

  Do not fall off the other side of the horse and never ask *any* questions! Ask appropriate questions as a sign of respect and interest, but not as a means of entrapment and false empathy. Comments indicating that you know the essentials about their business are good; for those prospective customers which are public companies, get the annual reports. Read the chairperson's letter. Good companies have a clear-written mission; bad ones do not. The best companies follow through on the leader's comments; most do not. Indirectly test whether the customer decision-maker has "hot buttons" aligned to the company's promulgated mission statement.

- *Do not demo unless required; then do so cleanly and quickly.* Modern technology has a lot to answer for with regard to the assault on the senses. Don't overwhelm the buyer. Tell the story. Have a written presentation and wait for interest before demoing. Demo to close the order; do not launch into it. It tends to be a "me, me, look how smart I am/we are" thing. Be cautious here.

The first step in improving any high-tech approach is deteching the sales force. Stop the techno talk. "People talk" counts the most. What will all of this techno virtuosity do other than cost a lot of money, possibly blow up, drive the salesperson nuts, require a lot of feed and caring, and potentially make the salesperson the laughing stock of the company? Keep it simple. Nice, clean facts are appreciated and remembered.

As Tom Hopkins (1984) says brilliantly in *How to Master the Art of Selling,* "People buy with emotion and defend with logic." They want to be satisfied emotionally that this buy-decision is not just another dumb deal they should have passed on. They worry that the proposition is too good to be true; that it will cost a lot more than quoted. Use your facts to answer these key emotional questions. If you doubt the validity of this premise, just think about your purchase of most big-ticket things such as a car or a house. Didn't you worry: (1) it was "too much," (2) you would "change your mind" later, or (3) there is a better "deal somewhere?" Your customers are no different. Deal with these questions directly, not by trying to outdemo or outsmart them. The "techno-speak" approach just raises the anxiety level of the buyer—"Whoops, I am being taken again."

- *Good manners.* Good manners are universally appreciated by the customer. If they ask you to have coffee, have it. Take your coffee black; the fuss-free option will endear you to the buyer. Do not hassle the receptionist, secretary, or assistant. Brush up on your manners. Think of your visit as going to a foreign country. Don't be the ugly American. Fit in.

The pleasant, polite salesperson is all too rare a phenomenon. Cut the jokes; most buyers cannot remember the last funny one they heard. Watch out about crossing the line into personal subjects. Most buyers feel vulnerable enough without being questioned on private matters. Well-mannered people have the best luck in getting the second or third appointment.

- *Minimize or eliminate your corporate rulebook.* God used just Ten Commandments to run the world. Do not add more of your own rules for your customers. Be easy to do business with. Do not treat your customers as potential bad debtors. Check out whether you will sell them before you see them; no credit applications should ever be inflicted upon potential customers in this day and age. Enough information is available today to get a D&B (Dunn & Bradstreet report) on most customers. At a minimum, you should know a few vendors that they buy from to check out credit, if required. Casual inquiry can get you their bank and a trade reference or two.

The Credit Applications department often seems to be a sorry institution intent upon harassment and putting customers "in their place." All of that customer credit information is available elsewhere. Once you get the customer's first check, you have access to all of it anyway. Do not be self-deceived; most credit managers do not do your firm any good. Otherwise, why the large bad debt balances? Big bad debts occur because credit managers do not check back on the story with your customer base. You do not lose money on new customers. You lose money on good customers that go bad—and the folks in credit rarely pay attention. So don't try to bail out your credit department by harassing prospective customers with forms. Excellent examples of this credit manager failure are Pharmor and Ames. Both showed signs of huge problems 18 months before going into Chapter 11 bankruptcy reorganization.

Find out customer needs; get the order written; and then fight with your beloved credit department to get the order approved. Do not waste time on jamming a rulebook down the customer's throat. If you handle the first part successfully, you can usually get the customer to conform to a few relatively minor rules later on.

- *Practice and refine your pitch.* It is imperative you keep working to refine your presentation. Find out from buyers afterwards what worked and what did not. Be careful about the analysis since a lot of success comes from emotion and that is both hard to describe and hard for people to admit they are susceptible to. Again, as Tom Hopkins (1984) says, "People buy with emotion and defend with logic."
- *Be organized.* Let us reemphasize some details. Use a contact manager software tool such as ACT! Have your travel case packed. Use the big salesperson type of travel case—it looks serious and there is always room for one more thing. Always have your data there so you can fill out the forms on the spot, close the deal, and get the order.

Again, with reference to Veblen and the desire to be above "actual work"—most salespeople like to look sleek with a small, thin briefcase. They never have the information required to complete the deal. Buyers love the information right there. Brown comments, "As one buyer said to me as I pulled one thing after another out of my salesperson case, 'Got a corn muffin in there too?' He loved the joke; told it often; and loved all the data I packed in the case. He especially liked it because I was the president of the company and thought enough of him to pack completely for the sales call. Do not let Veblen get to you here. Have the nitty-gritty with you."

## Real-World Lessons

Co-author Deaver Brown is the consummate salesman—a closer who generally gets the purchase order. Someone who's been selling his whole life, Brown held part-time sales jobs during his college years. After earning his MBA, he worked at General Foods, marketing Cool Whip (differentiated brand) and then Birdseye Vegetables (commodity "plus" brand). After a couple of years in the cocoon of Mother GF, he was bitten with entrepreneurial fever. In the 1970s, he sold baby goods (Cross River); in the 1980s–1990s, he sold UPS units for PCs (American Power Conversion); and in the 1990s–2000s, he sold low-cost, general interest information via CD-ROMs (Simply Media). These experiences provide a context for understanding how to "close" in the selling process and obtain the purchase order.

### *What Was Learned from the Cross River Umbroller Stroller Experience?*

Addressing the juvenile furniture marketplace, Brown cofounded Cross River, Inc. (CRI) in 1971 to manufacture, market, and sell the then-revolutionary stick-folding baby strollers to Macy's department stores, the Bloomingdale's of their day, and K-Mart, the Wal-Mart of its day. What were the lessons learned?

- *Pick names with a good image.* Brown picked "Umbroller" as a contraction of umbrella and stroller, and the name was extremely well-received. "Cross River" derived from a sign on 84 Route North in New York, a local town near the plant. It had the perfect 18th-century sound to help disguise the venture's newness.
- *Analyze and understand the size and structure of the market.* CRI determined that 1,400,000 baby strollers were sold annually according to the 1970 Census. Total wholesale sales were about $25 million. Despite the visibility of the category, with products rolling down the streets, the market was quite small, fragmented between 20 manufacturers, and the birth rate was in decline in the 1970s with only 3 million babies born per year (most purchases were for the first born; the rest hand-me-downs; first-born births were about 1,400,000 as well). CRI determined it was also a niche market with only 5 percent of the population at any time having any need whatsoever for a baby stroller in their family or extended family.
- *Target accessible channels of distribution.* Initially, CRI was selling primarily through small stores, but had secured a few small chains such as Bradlees in New England with 100 stores and, eventually, Wal-Mart, then having only 60 stores. The primary method of distribution was through the major chains, Sears, Wards, K-Mart, and JC Penney—very similar to Wal-Mart, Target, and Sears/K-Mart of today. A secondary form of distribution was through the growing regional discount chains, most of which have now been severely marginalized or gone out of business, such as Ames, Bradlees, Caldor, Hills, and Zayre. In the 1970s, department stores were a formidable force and had representation by stand-alone retailers in most major towns and cities in the United States. These outlets would later become marginalized, rolled-up into May or Federated, and stop selling anything but apparel. In the 1970s, outlets like Macys were an important influence and sold a lot of strollers.
- *Know the product costs.* The production costs worked out to be $8.00 per stroller in small quantities and declining to about $6.50 each for 10,000 units per month. The assembly process was reasonably complex with a frame consisting of 12 pieces of tubing, 8 wheels—2 per strut, 42 rivets, a specially sewn seat that had to be free-hanging, plastic-dipped handles to be cool in summer and warm in winter, various steel brackets to hold the product together, and a flexible footrest.
- *Set a price that assures a profit.* CRI sold $13.50 per stroller which retailed at $25.00 representing a 40 percent markup for the retailers. Some stores like Saks sold the Umbroller Stroller for $30.00. CRI's variable cost came in at $9.35; $8.00 for the stroller; 5 percent of the sales price ($13.50) for commissions, and 5 percent for other discounts, returns, and the like. So CRI netted $4.15 per stroller.
- *Know the operation's break-even.* Within a year, CRI was selling 2,000 strollers a month, enough to break-even on the entrepreneurs' low overhead costs. Knowing the break-even volume allows the entrepreneur to have information to make better decisions.
- *Set up a rep network.* Distribution did not seem unduly difficult with a very fragmented system. There were free-standing stores in most states; no major competitor that could stop CRI; lots of independent reps to help. The CRI entrepreneurs very early on attended their first trade show and got purchase orders for about 2,000 strollers, a one-month breakeven. Such early success in "closing the deal" provided a certain cachet that allowed them to attract and hire a group of commissioned sales reps around the country, and even landed an opening order from Bradlees, a small discount chain in New England.
- *Land a major account.* CRI's challenge was to land a major account to reach the 4,000–6,000 unit per month to get operations out of "the land of the living dead." CRI figured the old-line retailers would not budge. CRI was new and so was by definition "bad." CRI felt that the Young Turks were the discounters, trying to get big and successful. CRI had sold to Bradlees and that had gone all right; but the buyer left and the new buyer didn't give CRI much more business. CRI also saw an opportunity with department stores that flourished picking up new and interesting lines of merchandise. CRI had done well with them in a lot of small cities, though not in New York, Chicago, or Los Angeles—the major cities of the time. CRI targeted two possible major accounts: Macy's in New York and K-Mart, the Wal-Mart of its day, in Troy, Michigan. (Brown closed on both!)
  - –Macy's was the Bloomingdale's and Neiman Marcus of its day (and before there were many specialty store chains) and was a dominant player in selected

markets across the country. The New York buyer would help CRI get into its Midwestern and San Francisco stores if CRI was successful in doing business with him. Closing this account would give CRI a prestige boost in the large cities where the population was still centered in the 1970s. Macy's also had outlets in surrounding suburbs, of course, but the real action tended to be in their downtown stores where women pilgrimaged to have the fun of the shopping experience. The buyer was willing to see CRI because of past discussions and because he had seen the Umbroller Stroller in some of the smaller department stores in town. Further, he had an ongoing relationship with CRI's salesman who had sold him carriages, a big business in cities in those days. The buyer was a long-term employee and of a conservative nature. He was quite knowledgeable about the industry and Macy's methods and objectives.

–K-Mart was the lead dog in the industry. It was at least five times larger than its next competitor, Zayre, in New England, and the Woolco division of Woolworth in New York. K-Mart had no pretension of high-end merchandise and positioned its products toward blue-collar workers. If others, lured by the cachet of value pricing, wished to buy there so be it.

- *Price points.* K-Mart had three strollers: $9.99; $19.99; $29.99. They took slightly more than 40 percent markup or paid their vendors about $5.90, $11.80, or $17.40 or thereabouts for these products. CRI knew K-Mart worked a little tighter on margin at the low end and higher at the high end. So CRI's first question was, "What price point to pitch at?"
- *Choosing the right slot.* The idea of going "up" was absurd. The high price points have all the bells and whistles and generally sell darn little stuff in the major discounters. They are there principally for show. They also are subject to be changed-out continually as the next big thing hits—which always does. So the second price point, $19.99, made sense. This was especially appropriate since K-Mart had pretty good sell-through even at $24.99. CRI's price at the $19.99 retail slot was $11.80. With a $9.35 variable cost at low margins (with $1.35 built into that figure for rep commissions, returns, promotions), a clean $11.80 would deliver between $2.45 and $3.80, or 20 percent gross margin up to 32 percent—not bad. One might overlook the notion that $11.80 is an acceptable number. If volume were to soar, as CRI desired, the $8.00 cost would drop further to $6.50 at a minimum. That meant the upside was a 45 percent margin. So why not do it? The largest problem can be ego. The entrepreneur might forget that the objective is to close the deal and create a favorable platform to grow from. Agreeing to the $11.80 CRT price point (and the $19.99 K-Mart price point), could create a platform for future trust and more purchase orders.

- *Picking up on hints from the decision-maker.* The K-Mart buyer was seasoned, conservative, and liked the status quo. He had become a millionaire through K-Mart stock options, a situation for which he was famous. Although loyal to K-Mart, he was clear about his objective to finish up his last couple of K-Mart years smoothly and retire. He said, "Don't make a special trip to see me." Brown had previously called him from the New York airport saying he was in town and could he see the buyer. Several times before the buyer had said, "No." The one time he said, "Yes," Brown flew to Detroit and saw him. Since this buyer didn't like sales reps, Brown went alone. He told Brown this was an *informational* meeting only. Brown determined he would therefore inform him. The buyer said 10 minutes would be enough. That was a "buy sign." Brown indeed got the order. Did he know why? Not really! It is about *getting the order,* not explaining the rationale. It is about *listening* to the customer. And this brings the reasoning full circle as to why the entrepreneur must lead the sales charge. He or she must listen intensely, and often painfully, to buyers' responses to recalibrate the company's products, services, and organizations, as well as its presentations and selling habits. The sale to K-Mart was the beginning of this lesson for Cross River. CRI gradually learned what K-Mart "really" wanted: An aggressive packaging goods orientation to the staid baby furniture business. It took years before the buyer admitted to Deaver, "I bought from you in hopes you would drag the industry by its ears out of the dark ages of all the brown packaging and products of yesteryear."
- *Exploit the first key orders to establish long-term sustained relationships.* CRI got the initial POs from both Macy's and K-Mart. The trick is to make the opportunity snowball.

–The Macy's unit was also slotted at $11.80 for CRI, $19.99 for Macy's, providing Macy's with a 42 percent gross margin. From an initial test order of 100 units, the ongoing relationship flourished for well over a decade, until they discontinued hard goods.

–CRI closed the initial K-Mart deal for only 48 units in a four-store test, of 12 pieces per store. Within a year, however, K-Mart was buying 25,000 units per year. Within three years, 50,000 units; and the bragging rights helped catapult CRI to a 40 percent market share or 560,000 units per year. The lower price point expanded the market substantially and the company soon sold 1,000,000 units per year as the market expanded.

### *How Was the American Power Conversion Corp. (APCC) Experience Different?*

American Power, founded by three MIT engineers, created the small–sized Uninterruptible Power System (UPS) to capitalize on the growing importance of PCs in the early 1980s. With Moore's law doubling chip speed every 18 months, PCs were about to replace minicomputers in the workplace because they were simpler and easier to operate. Managers and entrepreneurs were preparing spreadsheets (Lotus 123) on their new processing tools.

The sales and marketing challenge was to locate the right distribution channel through which APCC could gain early dominance, and grow with the market to a substantial size. Interestingly, that market had not been created yet. The VARs (value-added resellers) were the ideal customers, but were just coming into being, putting together entire systems for companies. The first inkling of VARs emerging was with VARs selling point-of-sale and inventory control software, hardware, and peripherals to retailers.

This was a perfect market for APCC since retailers had important data to protect and lots of locations, which meant both a substantial need and lots of potential orders. While this was all transpiring, coauthor Brown led the effort to stabilize sales by selling to small computer retailers, distributors, and direct end-users. The effort was quite difficult and produced modest results in the early years; however, APCC's early entry to the VAR market meant the company ultimately kept its market leadership role as PC sales grew. The purchase orders eventually started rolling in. Profitable growth soon resulted. To help fund this growth, coauthor Levangie brokered through Wall Street APCC's IPO. The happy end to this selling story is that APCC is now at the $2 billion revenue level and has a $4.5 billion market capitalization.

### *What Market Traits Make the Current Simply Media Selling Experience Different?*

Simply Media (SM) experienced brand consumer software sales channel challenges similar to that of APCC. The primary area in which consumer products were sold was the mass market grocery, drug, and mass merchant retailers segments. Most software was too high-priced to sell well in these locations. As a rule, nothing much more than $5 sells well in groceries or drug chains (other than drugs themselves), and not more than $10 in mass market retailers.

This was best reflected in the fact grocery and drug chains sold 40 percent of the books and magazines sold at retail while they sold less than 1 percent of the software. This 39 percent differential was very appealing as a sales opportunity. The first step was to engineer costs out of the product system to reduce a $7.99 low-priced line aimed at computer stores such as Best Buy, Circuit City, and CompUSA and drive the price down to the $2.99 to $3.99 level.

As CEO, co-author Brown set up a series of rep groups to assist in this effort, but, as with Umbroller and APCC, they were of limited value since reps are best at servicing existing accounts, not opening them. Once he got the price point down to $3.99, Brown started to get modest distribution in these channels that includes grocery, drug, and mass market chains—opening up some sales with Kroger, Ahold, and RiteAid. Even though SM's sales were small, it became the leader in this distribution channel—the key to long-term survival—market share dominance—and being #1 or #2, as Jack Welch preached to the American business community (Peter Drucker agreed; so this wasn't bad company in which to be aligned).

As SM's made cost-saving improvements and gained outright ownership of its own titles (which its primary $9.99 price-slot competitors did not), its cost structure was reduced further so it could then sell the fastest-growing sector in retail—the dollar stores and dollar zones within multiple price point chains.

No software company had yet entered the dollar zone. SM therefore figured that if it reached this price point, the company would gain early dominance and establish brand image. In most consumer markets, this leads to long-term dominance (whoever really replaces M&Ms, Crest, Cool Whip, Cheerios, Rubbermaid, and the rest, despite the repeated blunders of their management teams?).

Simply Media accomplished dominance by reconfiguring its products into thin colorful sleeves for its CDs; selling only in preassorted displays; and emphasizing large order customers, but supplying smaller ones if they made the supply issues simple. The SM brand became the market leader in the $1 software business.

## Parting Thoughts

### *Does the Entrepreneur Remember How Professional Investors View Sales?*

Wall Street is constantly on the prowl for growth companies. Wall Street is notoriously unforgiving about failures. Wall Street forgives a lot with regard to fast-growing sales companies because increased sales cover a lot of sins in other areas. Wall Street is always trying to hitch its star to the "next" '49er's Gold Rush, whether it be multimedia a few years ago or the Internet today. Why? Because emerging markets produce all kinds of large, financially successful companies.

Many companies have grown quickly without any genuine profits at all. This is because their financial backers have allowed them the luxury of growing by subsidizing their lack of profit and usually their even greater lack of cash. Why do hard-boiled financial types permit this? Simply because sales are the top line that create the bottom line. Without substantial, growing sales, a company is apt to decline into mediocrity, to be followed by slow attrition and eventual extinction. The long-time credo of the Boston Consulting Group (and its many offshoots) is that profitability is a function of market share. Sales growth is key!

*Tip:* Don't ever forget that good sales performance keeps companies fresh, profitable, and happy! Too many entrepreneurs and executives forget this. Just get the purchase orders! Happy investors make for happier entrepreneurs!

### Does the Entrepreneur Remember to Keep an Open Mind to Allow Opportunities to Flow in?

Every business started with its first sale. Virtually every entrepreneur remembers his or her first sale as people remember their first love. Coauthor Brown, for example, recalls:

> My first sale in my own company was a 600-piece Umbroller stroller order to Bradlees, a major Massachusetts discounter at the time. I remember the buyer, Barry Cohen, the place, a corner of a One Park Avenue Showroom in New York City, and the circumstances—the quick demo, the sales negotiation, and getting the paperwork (before computers, one could actually get orders on the spot). This order was my initial training ground at my first trade show. After each order, or nonorder, I reviewed my success or failure, revised my approach, and pushed on. By the end of this first five-day trade show, I was much more effective by being more responsive to buyer needs, quicker off the mark, and faster to close.

The objective is to adjust continually your selling approach to be more responsive to customers and more effective in closing. This comes from listening to your customers with an open mind about everything surrounding the sale, and responding with better information, processes, and products or services. Each selling experience has the potential to give you more knowledge to move forward and be a better salesperson. You can either "dig in" and get ornery, or be one of those rare salespeople that stay fresh by being open to the new experiences and knowledge that is newly available to them.

*Tip:* You have two ears and one mouth—use them in proportion. Bad salespeople seem to have two mouths and one ear.

### Does the Entrepreneur Fully Realize that the Customer Is a Gold Mine Whose Ideas Can Lead to Additional Purchase Orders?

All customers have a potentially mutual stake in the outcome of the sales call. They can become the salesperson's partner. Remember, your customers have horizontal knowledge; you only have vertical knowledge. Retail and large industrial buyers see virtually all the important industry players every 90 days. They hear and are told virtually every industry story. This gives them a breadth of knowledge even they do not always appreciate. You, on the other hand, are caught in your vertical world of knowing your company very well, but not knowing as much about your competitors and their plans.

Buyers will rarely tell you directly about your competitor's plans. But they will respond to what they think will work best; much of this knowledge comes from their horizontal knowledge. Access this knowledge. Use it.

Timing is key. The above advice regarding intelligence gathering is to be used only *after* you have made your presentation, have their commitment to the concept, and then are filling in the details. Potential customers hate to be cross-examined or buried in questions.

The customer feedback and advice that the entrepreneur does receive can be quite constructive since it means that there is a seriously committed buyer who shares an interest in refining the deal so it is the best it can possibly be.

### Does the Entrepreneur Know "the Deal?" If Not, Why Not, and What's the Damage of Being "Off-deal" (Wal-Mart Example)?

Just consider Wal-Mart's profitable growth generated under Sam Walton's leadership. Mr. Sam spent a seemingly inordinate amount of time telling the Wal-Mart story ("the Deal") to his customers, suppliers, salespeople, bankers, Wall Street, and communities at large. His deal for consumers was the lowest price; his deal for everyone else was to share in the glow of the resulting prosperity coming from satisfied consumers. The proof about the power of Walton's simple, clear message was the fervor of the commitment he created. Just as clearly, once Walton was slowed down with cancer and gradually became less associated with Wal-Mart prior to his death, the company slowly became just another big firm mired in controversy with no special feeling around it. The Deal had been forgotten!

Now many communities sue Wal-Mart about siting new stores. People fear Wal-Mart, wary that their newly earned killer reputation will harm the local economy. Vendors fear Wal-Mart because Wal-Mart is exercising its muscle with tough terms, markdown money, chargebacks for small mistakes, and aggressive price negotiations. In other words, Wal-Mart now has the tough guy image that Sears had in the 1960s and 1970s which brought them low.

The final problem is all of this has slowed down Wal-Mart's sales growth. This, in turn, has slowed down its stock performance making employee stock options represent less value. So employees may become less committed in the field and at headquarters. A Wal-Mart job is no big deal now. As a result, the dry rot continues—just like it did at Sears in the 1960s and 1970s. It can be argued that the company no longer "knows the deal!" It has made the company vulnerable. Consider the four rules put forward by Maier (2005) on how to beat Wal-Mart:

1. *Hit 'em where they ain't.* Costco targets a higher economic demographic segment—people with cash who want cachet on the cheap. Result (2004): Costco sales per store was $115 million; Sam's Club was $67 million.
2. *Outdiscount the discounter.* Dollar Tree tries for straightforward pricing and a less painful shopping experience. Result (2004): Dollar Tree enjoyed a 9.7 percent operating margin; Wal-Mart's was 5.9 percent.
3. *Recreate what "the Deal" used to be.* In the grocery segment, Save-A-Lot stores bring back the old-time sense of Main Street and focus on underserved neighborhoods. Result (2004): Save-A-Lot's profit margin was 3.5 percent; Wal-Mart's was 2.6 percent (groceries only).
4. *Win the service game.* Dick's Sporting Goods has developed in-store sales teams that have both in-depth product knowledge and treat customers with TLC. Result (2004): Dick's Sporting Goods experienced revenue growth of 34 percent; Wal-Mart's was 16 percent (sporting goods only).

The player with the best "deal" generally wins.

## Does the Entrepreneur Know How to Define a Selling Proposition by What His or Her Company Does Not Do?

In reviewing successful companies, one is struck by the clarity of their deal proposition. Hertz rents cars, McDonalds sells hamburgers, H&R Block does your taxes, Southwest Airlines offers low cost travel, PricewaterhouseCoopers does corporate taxes and accounting, TRW makes parts, H-P develops computer-related products and instruments. GE stands out as the exception that proves the rule—that rare company that does many things well.

Successful companies generally offer excellent quality at a reasonable price. Many may have slightly higher prices than their competitors, but not by much. Each one has a solid value proposition. Occasionally they wander from their mission. This "wandering-off-deal" syndrome erodes the selling proposition.

An amusing case-in-point relates to the fast food business. McDonalds and Burger King joust with each other on premiums, new products, and the like. Yet, when desperate for increased sales and profits, every six months or so, they return to their low cost/high value roots and just put out lower prices on their basic menu. And, about a month later the CEO appears in the *Wall Street Journal* stating, with some surprise, "It worked. It really did." There is better food than McDonalds and Burger King; but quick, courteous service, and low costs got them to the party. Forget your deal at your peril, folks.

Just consider the failure of Sears (before Arthur Martinez) and later K-Mart to retain the ranking as the number one American retailer. Good quality at a great price got them to the party and to the highest industry ranking. They then started to nibble at the edges of their "Deal." They took a spoke out of a bicycle here, a double stitching out of a garment there, and replaced a brand name with a no-name over there. Then the price of the goods moved up a percentage point over here, then over there, then overall. Result: They forgot their *deal.*

The consumer does not catch on all at once. The first thing that goes is excitement about shopping there. People waited for their Sears catalog; they checked it out before buying almost anything, anywhere. That excitement disappeared decades ago. The catalog only expired a few years ago. Leadership was lost when the excitement disappeared.

The same "wandering-off-deal" happened at K-Mart. The company stopped looking for great value for their customers. They discontinued their blowout pricing. And they became just another store.

As detailed previously, the same thing is happening at Wal-Mart these days. As one consumer who went into a new store said, "I was expecting something special; it was not there." The success or failure of Wal-Mart's 2006 image campaign ("Look beyond the basics!") remains untested.

The entrepreneur-salesperson must acknowledge this reality of knowing what you aren't. You must know what you *don't know!*

The best example of this approach is Southwest Airlines. They focus on value and revel in *what they are not.* This permits them to be the best at what they are. The founder realized that his number one customer was his employees. He realized that if he let his customers destroy the morale of his employees, they would not be able to do their job well.

As a result, every Southwest employee is permitted to, in effect, "Fire a Customer." The method is not to say to the customer, "You are wrong." The approach is to say, "We don't do that here. You should try our competitor, American. They do what you want."

The Southwest "deal" is to provide low-cost transportation competitive with cars. It is meant to take salespeople, families, and others off the road and load them onto planes because Southwest is cheaper and faster. Period. That is the deal. Southwest does not compete with other airlines. Those carriers simply happen to be there, too.

To execute this "deal," along with their enviable excellence in safety and on-time arrival performance, Southwest decided what they would *not do:*

1. *No food.* That requires clean up and expense. Food slows down the turnaround time at airports so planes cannot be used as often and elimination of food service decreases expense.
2. *No assigned seats.* This eliminates the complexity, the hassle, the error rate, and the upset. It speeds up loading and requires fewer staff people, hence less expense.
3. *No third-party ticket distribution.* This eliminates the fees and errors with travel agents.

This definition of deal also makes the whole enterprise a more efficient one because employees can concentrate on fewer things. Just as importantly, employees have the ability to say honestly, "We do not do that here. If you want food, assigned seats, and tickets through other people, go to American. If you want fast, dependable, cheap service—we do that."

As Tom Peters says in one of his books, "The Wow factor is important." Southwest? …..Wow!

## *Does the Entrepreneur Know How to Present, Close, and Leave?*

In a sales presentation, you need to focus on the other guy—not your notes. You need to master the details so you can listen patiently to the buyer's questions and respond accordingly.

Brown observes:

> In my sales presentations, I find myself always trying to head for the exit once the order is committed to. I do not want to give the slightest sliver of opportunity for a rethinking, a new discussion, or a thoughtful moment. My best reps know that my skill in getting out of an office quickly after the order is committed to is my most memorable talent. Get the order—leave. Let the customers consider this settled ground; move on. Give them their time and space.

And this brings the discussion full circle as to why the entrepreneur must lead the sales charge. He or she must listen intensely, and often painfully, to buyers' responses to recalibrate their products, services, and organizations, not to speak of their presentations and selling habits. Message: Close and leave.

## *Does the Entrepreneur Remember the Dream and the Payoff?*

The good entrepreneur truly believes in his or her dream and is a missionary to convert all the nonbelievers. If the selling process is well-executed, the purchase orders will roll in. What's the payoff for all the nitty-gritty tasks of customer prospecting? Consider these sales of entrepreneurial companies, as reported by Howard (2006) and Reidy (2006):

- Tom's of Maine (natural products, such as toothpaste) sold itself to Colgate for $100 million in 2006.
- The Body Shop (2,085 stores—environmentally friendly products) was bought by L'Oreal for $1.1 billion in 2006.
- Cape Cod Potato Chips was sold first to Eagle Snacks (1985) and then (after repurchase) to Lance, Inc. (1999).
- Nantucket Nectars was sold first to Ocean Spray (1997) and then to Cadbury Schweppes (2002).
- Ben & Jerry's was sold to Unilever in 2000.
- Stonyfield Farm was sold to French Dannon yogurt maker Groupe Danone in 2003.

So why all the fuss over purchase orders? As they say at MIT, it should be intuitively obvious to even the most casual observer!

## References


Banks, E. Douglas. 2005. How-to book. *Boston Business Journal* (May 27–June 2)

Baty, Gordon B. 1990. *Entrepreneurship for the nineties.* New Jersey: Prentice Hall.

Bhide, Amar, and Brown, Deaver. 1993. *Deaver Brown and Cross River, Inc.* Harvard Business School Case Study N9-394-042.

Brown, Deaver. 1980. *The Entrepreneur's Guide.* New York: Ballantine Books.

Collingwood, Harris, and Coutu, Diane L. 2002. The HBR interview—Jack on Jack. *Harvard Business Review* (February).

Drucker, Peter. 1964. *Managing for results.* New York: Harper & Row.

Exley, Helen. 1993. *The best of business quotations.* New York: Exley Gift Books.

Gellerman, Saul W. 1990. The tests of a good salesperson. *Harvard Business Review* (May–June).

Goodman, Ted. 1997. *The Forbes book of business quotations.* Black Day and Leventhal Publishers.

Hexner, Lila M. 1987. *Start-up guide.* Smaller Business Association of New England.

Hopkins, Tom. 1984. *How to master the art of selling.* Warner Books.

Howard, Theresa. 2006. Big companies buy small brands with big values. *USA Today* (March 22).

Maier, Matthew. 2005. How to beat Wal-Mart. *Business 2.0* (May).

McKay, Edward S. 1972. *The marketing mystique.* American Marketing Association.

Miller, Robert B., and Stephan E. Heinman. 1986. *Strategic Selling.* New York City: Harper & Row.

Reidy, Chris. 2006. Colgate will buy Tom's of Maine. *The Boston Globe* (March 22).

Veblen, Thorsten. 1970 (1899). *The theory of the leisure class.* Augustine M. Kelley Publishers.

Willigan, Geraldine E. 1992. High-performance marketing: An interview with Nike's Phil Knight. *Harvard Business Review* (July–August).

## About the Authors

**Deaver Brown** (deaver@simplymedia.com) is CEO and publisher of *Simply Magazine,* with the Simply Media brand (simplymedia.com). He has concentrated on founding/cofounding mass market consumer product companies such as Cross River, Umbroller stroller (sold to Rubbermaid), American Power (NASDAQ-APCC), and *Simply Magazine.* He wrote *The Entrepreneurs Guide* (Macmillan; Ballantine), now an interactive CD, and *Business Startup.* He has authored several interactive CDs available in retail stores and simplymedia.com (*Business Startup; Legal Forms & Guide; Sales Skills; Negotiations Handbook; Finance Your Business; Manage Your Home Office; Starting Your Career*). Brown's case study, "Deaver Brown and Cross River Inc.," coauthored with Professor Amar Bhide, is widely used in MBA programs worldwide. He earned his AB and MBA at Harvard

**Joseph Levangie** (joe.levangie@comcast.net) is a Boston-area investor, adviser, and entrepreneur. Over the last quarter century, he has helped launch several dozen new business enterprises from first a large company platform, then from a not-for-profit incubator, and later as an venture adviser, as an independent entrepreneur, as an active investor and as a passive "angel." His companies have competed in a wide array of industries: financial services; renewable energy; uninterruptible power sources; biotech; computer hardware, flex circuits and software; medical lasers; electronic retail color-matching systems; radioactive medical implants; food technology; modular housing; semiconductor equipment; specialty materials; and waste tire recycling. The number of Levangie's ventures successfully completing an IPO has now reached double figures. Levangie has served on the boards of directors of dozens of private and public companies, and has been a guest reviewer at Business Plan contests at MIT and Harvard Business School. Joe is an active alumnus of both institutions. Levangie currently is vice chairman of Ardour Capital Investments, a New York City investment banking firm.

*New England Journal of Entrepreneurship*
John F. Welch College of Business
Sacred Heart University
5151 Park Avenue
Fairfield, Connecticut 06825-1000

*New England Journal of Entrepreneurship* Volume 9 Number 1 Spring 2006